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Federal Communications Commission

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Before the
FEDERAL COMMUNICATIONS COMMISSION
 Washington, D.C. 20554

DISPATCHED BY

In the Matters of)	
)	
1998 Biennial Regulatory Review --)	CC Docket No. 98-81 ✓
Review of Accounting and Cost)	
Allocation Requirements)	
)	
United States Telephone Association)	ASD File No. 98-64
Petition for Rulemaking)	
)	
Implementation of the)	
Telecommunications Act of 1996)	CC Docket No. 96-150
Accounting Safeguards under the)	
Telecommunications Act of 1996)	
)	
Petition for Forbearance of the)	
Independent Telephone &)	AAD File No. 98-43
Telecommunications Alliance)	
)	
Petition for Rulemaking to Amend Part 32)	
of the Commission's Rules, Uniform System)	RM-9341
of Accounts for Class A and Class B Telephone)	
Companies, to Adopt the Accounting for)	
Software Required by Statement of)	
Position 98-1)	

**REPORT AND ORDER IN CC DOCKET NO. 98-81,
 ORDER ON RECONSIDERATION IN CC DOCKET NO. 96-150,
 FOURTH MEMORANDUM OPINION AND ORDER IN AAD FILE NO. 98-43**

Adopted: May 18, 1999

Released: June 30, 1999

By the Commission: Commissioner Ness issuing a statement, Commissioner Furchtgott-Roth dissenting in part and concurring in part and issuing a statement, Commissioner Powell concurring and issuing a statement.

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I. INTRODUCTION

1. In this Order, as part of our biennial review under section 11 of the Communications Act of 1934, as amended (Communications Act),¹ we adopt the proposals set forth in our June 17,

¹ 47 U.S.C. § 161.

1998 Notice of Proposed Rulemaking (*Accounting Notice*).² Specifically, we streamline the accounting requirements for mid-sized incumbent local exchange carriers (ILECs) whose aggregate annual revenues are less than \$7 billion by allowing these mid-sized ILECs, currently required to use Class A accounts to use the more streamlined Class B accounts. Consistent with our change in the level of accounting detail required, we conclude that mid-sized ILECs should also be permitted to submit their cost allocation manuals (CAMs) based on the Class B system of accounts, thereby reducing the reporting burden of carriers subject to CAM requirements. In addition, mid-sized ILECs will now only be required to obtain an attestation every two years, instead of an annual financial audit requiring a positive opinion. We note that our actions in this Order do not supersede the states' treatment of mid-sized carriers, and therefore do not in any way change existing state authority over state accounting and cost allocation requirements of mid-sized carriers.

2. We reduce or eliminate a number of other accounting requirements for all carriers subject to Part 32 of the Commission's rules as follows: we combine accounts 2114, 2115, and 2116 into a single new account 2114; we combine accounts 6114, 6115, and 6116 into a single new account 6114; and we eliminate account 5010 and require all nonregulated revenues to be recorded in account 5280. We eliminate the requirement in section 32.16 for filing projected future effects of an accounting change. We also eliminate the requirement in section 32.2000(b) that carriers submit for Commission approval journal entries made to record acquisitions from other entities of telecommunications plant that cost more than \$1 million for Class A carriers and \$250,000 for Class B carriers.

3. In addition, we address one issue in a Petition for Reconsideration³ of our *Accounting Safeguards*⁴ proceeding regarding electronic publishing affiliates' compliance with the section 274 requirements. In this Order, we modify our holding in the *Accounting Safeguards Order* and conclude that the information contained in the limited version of the Securities and Exchange Commission's (SEC) Form 10-K, with certain modifications, is sufficient to enable the Commission to monitor electronic publishing affiliates' compliance with the section 274 requirements.

4. In this Order, we grant a significant portion of the relief requested by Independent Telephone and Telecommunications Alliance (ITTA) in its petition for forbearance.⁵ For example, as

² 1998 Biennial Regulatory Review -- Review of Accounting and Cost Allocation Requirements, CC Docket No. 98-81, *Notice of Proposed Rulemaking*, 13 FCC Rcd 12973 (1998). Appendix A contains a list of parties filing comments and reply comments and their abbreviated names in CC Docket No. 98-81 and ASD File No. 98-64, the United States Telephone Association (USTA) Petition for Rulemaking.

³ Petition for Reconsideration of SBC Communications, Inc., filed Feb. 20, 1997.

⁴ *Accounting Safeguards Under the Telecommunications Act of 1996*, CC Docket No. 96-150, *Report and Order*, 11 FCC Rcd 17539 (1996) (*Accounting Safeguards Order*).

⁵ ITTA lists nine issues for which they request forbearance. Petition for Forbearance of the Independent Telephone and Telecommunications Alliance, filed February 17, 1998 (Petition). The deadline for the Commission's action on ITTA's petition was extended by 90 days to May 18, 1999. See Petition for Forbearance of the Independent Telephone and Telecommunications Alliance, AAD File No. 98-43, *Order*, 14

requested by ITTA, we streamline accounting requirements for mid-sized ILECs to permit them to use the Class B system of accounts. Although we decline to forbear from requiring these carriers to file cost allocation manuals, to obtain independent audits of those manuals, and to maintain property records, in this Order we significantly streamline these accounting requirements for mid-size ILECs. We permit mid-size ILECs to submit their CAMs based on the Class B system of accounts, and we modify our audit requirements so that mid-sized ILECs will now only be required to obtain an attestation every two years. Thus, a significant amount of the relief sought by ITTA in the Petition for Forbearance is realized through the rule changes adopted in this proceeding.

5. We also address the issues raised in the Petition for Rulemaking filed by BellSouth and Bell Atlantic regarding the accounting for computer software costs and amend our rules to provide that the cost of all software must be recorded in conformance with generally accepted accounting principles (GAAP).

6. Finally, we recognize that our accounting and cost allocation rules need to be streamlined. We believe such changes should be carefully determined after the views of all parties, including those of state commissions, affected by the changes have been considered.⁶ As we announced in a recent Public Notice,⁷ the Common Carrier Bureau is initiating a broad and comprehensive review of its accounting and reporting requirements. The comprehensive review will be undertaken in two phases. Phase 1, which has already begun and will conclude by the end of the year, will address current accounting and reporting requirements that can be eliminated or streamlined in order to minimize the burdens on the industry while retaining sufficient information needed for the

FCC Rcd 1018 (1999). In this Order, we address ITTA's forbearance request regarding the financial reporting and recordkeeping requirements. The remaining issues raised by ITTA are resolved in separate proceedings. See Amendment of the Commission's Rules to Establish Competitive Service Safeguards for Local Exchange Carrier Provision of Commercial Mobile Radio Services, Implementation of Section 601(d) of the Telecommunications Act of 1996, WT Docket No. 96-162, *First Order on Reconsideration*, Petition for Forbearance of the Independent Telephone and Telecommunications Alliance, AAD File No. 98-43, *First Memorandum Opinion and Order*, FCC 99-102 (rel. June 30, 1999); Petition for Forbearance of the Independent Telephone and Telecommunications Alliance, AAD File No. 98-43, *Second, Third, Sixth Memorandum Opinions and Orders*, FCC 99-102, 99-104, 99-105, 99-108 (rel. June 30, 1999); 1998 Biennial Regulatory Review – Review of ARMIS Reporting Requirements, Petition for Forbearance of the Independent Telephone and Telecommunications Alliance, CC Docket No. 98-117 and AAD File No. 98-43, *Report and Order in CC Docket 98-117, Fifth Memorandum and Opinion in AAD File No. 98-43*, FCC 99-106 (rel. June 30, 1999).

⁶ Broad revisions to our accounting and cost allocation rules will have an immediate and significant impact on state regulators. Moreover, the accounting issues involved will not only impact the Commission's Part 32 and 64 rules, but also our Part 36 jurisdictional separations rules, as well as ongoing universal service and access reform proceedings. For these reasons, we do not, in this Order, propose broad revisions to our accounting and cost allocation rules. Such change requires evenhanded deliberation among all parties affected to produce results that are meaningful for these parties.

⁷ See "Common Carrier Bureau Announces Initiative to Undertake Comprehensive Review of Part 32 and ARMIS Requirements," *Public Notice*, DA 99-695 (rel. Apr. 12, 1999).

Commission and state agencies to meet their responsibilities.⁸ Phase 2, which will begin in the last quarter of 1999, will examine the current accounting and reporting structure and address long-term changes needed as local exchange markets become competitive, and will assess what, if any, interim measures should be made as competitive milestones are reached. During this process, the Common Carrier Bureau will continue to work closely with the National Association of Regulatory Utility Commissioners (NARUC) and state commissioners so that, in addition to eliminating unnecessary reporting requirements, the Commission and states will focus on further steps necessary to eliminate unnecessary overlap of Federal and state reporting requirements.⁹

II. BACKGROUND

7. *CC Docket No. 98-81 and ASD File No. 98-64.* On June 2, 1998, as part of our biennial review under section 11 of the Communications Act, we adopted our *Accounting Notice* to review and modify the Commission's accounting and cost allocation rules.¹⁰ We proposed to raise the threshold significantly for required Class A accounting, thus allowing mid-sized ILECs currently required to use Class A accounts to use the more streamlined Class B accounts.¹¹ In addition, we proposed to establish less burdensome CAM procedures for the mid-sized ILECs and to reduce the frequency with which independent audits of the cost allocations based upon the CAMs are required.¹²

⁸ See "Common Carrier Bureau Announces Agenda for Initial Workshop for Phase I of the Comprehensive Review of Accounting and Reporting Requirements and Treatment of Ex Parte Presentations in Related Proceedings," *Public Notice*, DA 99-758 (rel. Apr. 19, 1999). The initial workshop was Wednesday, April 21, 1999.

⁹ We note that in a recently adopted resolution, NARUC recommended improving the monitoring of telecommunications service quality by requiring standardized reports. See NARUC Resolution Adopting NARUC State Staff Service Quality White Paper, Adopted in Convention, November 11, 1998. The resolution recommended that ILECs and competitive local exchange carriers (CLECs) collect service quality data on a monthly basis and report such data to Federal and state regulatory commissions on a quarterly basis. This would make the service quality information accessible to the states to facilitate comparisons between jurisdictions. NARUC also urged the Commission to ensure that its program imposes only reasonably necessary reporting obligations on industry participants in order to effectively monitor retail telecommunications service quality.

¹⁰ The operation of our cost allocation rules serves to protect ratepayers from different concerns. The cost allocation rules provide guidance to carriers as to how joint and common costs are to be allocated among regulated and nonregulated activities. These rules are premised on the assumption that ratepayers benefit from the economies of scope associated with integrated operations of regulated and nonregulated activities. Because costs are recorded in regulated accounts, the Commission retains the ability to scrutinize costs associated with nonregulated activities. These procedures promote fair cost allocation and protect regulated ratepayers from absorbing the costs of nonregulated activities. See 47 C.F.R. §§ 32.1 *et seq.* and 64.901 *et seq.*

¹¹ See 47 C.F.R. § 32.11.

¹² Pursuant to section 64.903 of the Commission's rules, carriers with annual operating revenues equal to or above a certain threshold must file a manual with the Commission on an annual basis that contains certain information regarding its allocation of costs between regulated and nonregulated activities. Among other things,

We also proposed several changes to our Uniform System of Accounts (USOA) to reduce accounting requirements and to eliminate or consolidate accounts for all carriers.¹³ Finally, we sought proposals for other accounts or filing requirements that could be reduced or eliminated.¹⁴

8. *ITTA Petition for Forbearance.* ITTA is an organization of mid-sized ILECs with fewer than 2 percent of the nation's access lines. On February 17, 1998, ITTA filed a petition for forbearance on several issues.¹⁵ The first issue – that Class A accounting requirements, CAM filings, and audits for mid-sized carriers are overly burdensome and should be eliminated – is addressed in this Order.

9. *SBC Communications, Inc. (SBC) Petition for Reconsideration of the Accounting Safeguards Order.* In the *Accounting Safeguards Order*, we concluded that section 274 affiliates that already file an SEC Form 10-K must file a copy with this Commission.¹⁶ For those section 274 affiliates that were not required to file a Form 10-K with the SEC, we required them to file an identical form with us.¹⁷ SBC filed a Petition for Reconsideration asserting that a simplified report will satisfy the intent of section 274(f). In this Order, we only address the section 274 issues raised by SBC. The remaining issues, raised by SBC and other petitioners, will be addressed in another Order on Reconsideration.

10. *Bell Atlantic and BellSouth Petition for Rulemaking.* When the Commission adopted the USOA, we required that the original cost of operating system software be recorded in the same account as the associated plant rather than a separate software account.¹⁸ Later, the Commission directed that the cost of all software not considered initial operating system software (*i.e.*, application software) be recorded in conformance with GAAP, which could result in the expensing or capitalization of such software costs depending on the circumstances. On March 4, 1998, the

the CAM must include a description of each of the carrier's nonregulated activities and a statement "identifying each affiliate that engages in or will engage in transactions with the carrier and describing the nature, terms and frequency of each transaction." 47 C.F.R. § 64.903(a).

¹³ In doing so, we addressed USTA's Petition for Rulemaking, dated Sept. 16, 1997 (USTA Petition).

¹⁴ *Accounting Notice*, 13 FCC Rcd at 12984, ¶ 19.

¹⁵ *Petition for Forbearance of the Independent Telephone and Telecommunications Alliance*, filed February 17, 1998 (ITTA Petition). The deadline for the Commission's action on ITTA's petition was extended by 90 days to May 18, 1999. See *Petition for Forbearance of the Independent Telephone and Telecommunications Alliance*, AAD File No. 98-43, *Order*, 14 FCC Rcd 1018 (1999).

¹⁶ *Accounting Safeguards Order*, 11 FCC Rcd at 17645, ¶ 230.

¹⁷ *Id.*

¹⁸ See *Revision of the Uniform System of Accounts and Financial Reporting Requirements for Class A and Class B Telephone Companies* (Parts 31, 33, 42, and 43 of the FCC's Rules), CC Docket 78-196, *Report and Order*, 60 Rad. Reg. 2d (P&F) 1111 (1986) at ¶ 132; 47 C.F.R. 32.2000(i).

American Institute of Certified Public Accountants issued Statement of Position 98-1 (SOP 98-1) to provide authoritative guidance on accounting for the costs of computer software effective for financial statements for fiscal years beginning after December 15, 1998.¹⁹ SOP 98-1 generally requires the capitalization of software costs. On August 3, 1998, Bell Atlantic and BellSouth filed a petition for rulemaking to amend the Commission's existing Part 32 rules in order to accommodate these recent changes governing the treatment of software costs.

III. DISCUSSION

A. Revenue Threshold for Determining Level of Reporting for Mid-Sized ILECs

11. Currently, under the Commission's rules there are two classes of ILECs for accounting purposes: Class A and Class B.²⁰ Carriers with annual operating revenues from regulated telecommunications operations equal to or above a designated indexed revenue threshold, currently \$112 million, are classified as Class A; those with annual operating revenues below the threshold are considered Class B.²¹ The classification of a carrier is determined by its lowest annual operating revenues for the five immediately preceding years.²² Generally, Class A accounts provide more detailed records of investment, expense, and revenue than the Class B accounts. For instance, Class A carriers must record their transactions in 261 accounts while Class B carriers maintain 109 accounts. The difference in the number of accounts is due to the fact that many of the Class A accounts are aggregated into summary accounts under Class B. The Commission intentionally generalized the level of accounting required under Class B to accommodate smaller carriers while maintaining the necessary degree of regulatory oversight and monitoring needed for these smaller carriers.²³

12. In the *Accounting Notice*, we proposed to streamline accounting requirements for certain mid-sized ILECs based on the aggregate revenues of the ILEC and any ILEC that it controls,

¹⁹ American Institute of Certified Public Accountants (AICPA) Statement of Position 98-1, *Accounting for the Costs of Computer Software Developed or Obtained for Internal Use*, Issued by the Accounting Standards Executive Committee, March 4, 1998, at Summary.

²⁰ 47 C.F.R. § 32.11.

²¹ See "Annual Adjustment of Revenue Threshold," *Public Notice*, 13 FCC Rcd 11057 (1998) (adjusting annual indexed revenue threshold to \$112 million). "Annual operating revenues" includes revenues from both regulated and nonregulated activities, to determine whether carriers must file ARMIS reports and cost allocation manuals. See *Reform of Filing Requirements and Carrier Classifications*, CC Docket No. 96-193, *Report and Order*, 12 FCC Rcd 8071, 8102, ¶ 68 (1997) (*Filing Requirements Reform Order*); see also *Reform of Filing Requirements and Carrier Classifications*, CC Docket No. 96-193, *Order and Notice of Proposed Rulemaking*, 11 FCC Rcd 11716, 11732-34, ¶¶ 30-32 (1996).

²² See 47 C.F.R. § 32.11(e).

²³ See *Revision of the Uniform System of Accounts and Financial Reporting Requirements for Class A and Class B Telephone Companies* (Parts 31, 33, 42, and 43 of the FCC's Rules), CC Docket No. 78-196, *Report and Order*, 60 Rad. Reg. 2d (P&F) 1111 (1986) (creating Part 32 of the Commission's rules).

is controlled by, or with which it is under common control.²⁴ We proposed that if the aggregate revenues of these affiliated ILECs are less than \$7 billion, then each ILEC within that group would be eligible for Class B accounting, even if the annual operating revenue of any individual ILEC equals or exceeds \$112 million.

13. The large ILECs -- the Bell operating companies (BOCs) and GTE -- contend that Class A accounting is not needed and the Commission should adopt a single accounting system for all ILECs;²⁵ most of the remaining commenters support our proposal.²⁶ Several commenters observe, and we agree, that our Class A accounting requirements play a significant role in ensuring that all rates, including intrastate rates, remain just and reasonable.²⁷

14. We adopt the proposal in the *Accounting Notice*. Among ILECs, this revision would limit Class A accounting to the BOCs and GTE. All other ILECs may use the Class B system of accounts.²⁸ We believe we can satisfy our oversight responsibilities and meet the Commission's needs

²⁴ See 47 C.F.R. § 32.9000. Our rules define "control" as "the possession directly or indirectly, of the power to direct or cause the direction of the management and policies of a company, whether such power is exercised through one or more intermediary companies, or alone, or in conjunction with, or pursuant to an agreement with, one or more other companies, and whether such power is established through a majority or minority ownership or voting of securities, common directors, officers, or stock-holders, voting trusts, holding trusts, affiliated companies, contract, or any other direct or indirect means."

²⁵ See Bell Atlantic Comments at 7-9; BellSouth Comments at 9-12; US West Comments at 7; Ameritech Comments at 4-9; SBC Comments at 5-17; GTE Comments at 9-11. In addition, USTA recommends eliminating Class A accounting for all ILECs. USTA Comments at 6-11.

²⁶ See, e.g., CBT Comments at 2; ALLTEL Comments at 4; Comsat Comments at 1-2; Sprint Comments at 2-3; Texas PUC Reply Comments at 5-6.

²⁷ See, e.g., GSA Reply Comments at 6; MCI Comments at 3-5 & Reply Comments at 9; PUCO Reply Comments at 3; AT&T Reply Comments at 5-8; Texas PUC Reply Comments at 4-5; Florida PSC Reply Comments at 1-2; PaPUC Reply Comments at 7-8. The following are several examples of recent actions dependent on Class A accounting: In our *Access Reform* proceeding we modified Part 69 to assign maintenance expense to the central office switching based on Class A accounting that separately records maintenance expense for each major class of network facility. This significantly improved the assignment of cost to local switching and resulted in substantial shifts in permitted revenues between price cap baskets. In addition, we created a new basket for marketing expense. Class A accounting separates marketing expense from other customer operations expenses. In the *Expanded Interconnection* physical collocation tariff investigation we focussed on LEC assignments of land, buildings, and other support assets and expenses. This investigation of various common cost and overhead loadings would have been far more difficult without Class A account detail. In the *GSF Order*, we reassigned general purpose computers to non-regulated billing and collection which required the existence of Class A account 2124. Finally, in the *Number Portability* proceeding the charges will be established based on additional costs the LECs will incur to provide this additional network functionality. Class B accounts do not provide sufficient detail to identify portability related costs clearly.

²⁸ Carriers that qualify for Class B accounting may, at their discretion, maintain a Class A accounting structure upon the submission of written notification to the Commission. See 47 C.F.R. § 32.11.

by employing the more streamlined Class B account structure on mid-sized ILECs and retaining the more detailed Class A account structure for the largest ILECs at this time. As we discussed above, the Common Carrier Bureau has initiated a comprehensive review of its accounting and reporting requirements which will address current accounting and reporting requirements that can be eliminated or streamlined and long-term changes needed as local exchange markets become competitive. We note that the Commission has previously reduced reporting and accounting requirements imposed on interexchange carriers as competition in that market developed and we fully expect to provide similar regulatory relief in the local exchange and exchange access markets as circumstances warrant.

15. *Pole Attachment Fees.* The Commission reviews complaints about pole attachment rates under section 224 of the Communications Act.²⁹ In reviewing the rates charged by ILEC owners of poles, ducts, conduits and rights-of-way, the Commission applies data taken from ARMIS reports.³⁰ Under the Class B accounting structure we adopt for mid-sized ILECs, detailed accounts needed to calculate pole attachment fees using the pole attachment formulas would no longer be reported in their ARMIS reports.³¹ In our *Accounting Notice*, we sought comment on whether mid-sized ILECs should be required to maintain this accounting data in subsidiary records to report in ARMIS the information in the noted accounts as well as other information required by the pole attachment formulas.³² Although several carriers argue that a subsidiary record requirement is unnecessary,³³ we conclude that the mid-sized companies should continue to maintain this information in subsidiary records. We believe it is necessary to require subsidiary records to assure that the data is publicly available, uniformly maintained among the carriers, and maintained in a manner that can be audited. We therefore require mid-sized ILECs to maintain subsidiary record categories to provide the pole attachment data currently provided in the Class A accounts, and we require these carriers to report the information necessary for the Commission to calculate pole attachment rates based on their ARMIS reports.³⁴ We note that the Commission is currently considering issues regarding the pole attachment formulas.³⁵ When we issue a report and order in that proceeding, we will specify the

²⁹ 47 U.S.C. § 224.

³⁰ 47 C.F.R. §§ 1.1401-1.1416 (1997).

³¹ Class B carriers record their investment associated with poles in Account 2410 (Cable and wire facilities). Account 2410 includes the investment associated with poles, as well as the investment associated with aerial cable, underground cable, buried cable, submarine cable, deep sea cable, intrabuilding network cable, aerial wire, and conduit systems. See 47 C.F.R. §§ 32.2410-2441. Likewise, Class B carriers record their expenses associated with poles in Account 6410 (Cable and wire facilities expenses), which contains aggregated expense data related to aerial cable, underground cable, buried cable, submarine cable, deep sea cable, intrabuilding network cable, aerial wire, and conduit systems. See 47 C.F.R. §§ 32.6410-6441.

³² For example, the current and proposed pole attachment formulas require accumulated depreciation as detailed in ARMIS Report 43-02, Table B-5 for the Poles and Conduit System accounts.

³³ See GTE Comments at 13; SBC Comments at 6; Frontier Comments at 2; Sprint Comments at 4.

³⁴ See 1998 Biennial Regulatory Review – Review of ARMIS Reporting Requirements, Petition for Forbearance of the Independent Telephone and Telecommunications Alliance, CC Docket No. 98-117 and AAD File No. 98-43, *Report and Order in CC Docket 98-117, Fifth Memorandum and Opinion in AAD File No. 98-43*, FCC 99-106 (rel. June 30, 1999).

³⁵ See Amendment of Rules and Policies Governing Pole Attachments, CS Docket No. 97-98, *Notice of Proposed Rulemaking*, 12 FCC Rcd 7449 (1997). 9

subsidiary record categories carriers must maintain in order to provide data for the finalized pole attachment formulas.

16. *Jurisdictional Separations.* In the *Accounting Notice*, we asked commenters to address any possible effects on jurisdictional separations that could result from adopting our proposals.³⁶ We note that we are not changing our Part 36 jurisdictional separations rules today. In adopting the streamlined accounting rules for mid-sized ILECs, we recognize that certain costs will now be allocated between the state and interstate jurisdictions differently. As GTE and USTA observe, the mid-sized ILECs that become subject to Class B accounting will separate their General Support Facilities (GSF) investment between the state and interstate jurisdictions based on Combined Central Office Equipment, Information Origination/Termination, and Cable & Wire Facilities investment. Class A ILECs allocate GSF investment based on Plant Specific Expenses, Plant Non-Specific Expenses (network operations expenses), and Customer Operations Expenses (marketing and services).³⁷

17. *Application of Threshold.* In the *Accounting Notice*, we proposed eliminating the difference between the application of the indexed revenue threshold for Parts 32 and 64 because the difference provided unnecessary complexity to our rules. Although the same indexed revenue threshold is applied for Part 32 carrier classification purposes and Part 64 cost allocation purposes, the threshold is met at different times. For Part 32 purposes, the accounting classification for a carrier is determined by its lowest annual operating revenues from regulated operations for the five immediately preceding years. For Part 64 cost allocation purposes, however, carriers must file CAMs and obtain independent audits of their cost allocations based upon those CAMs once carriers equal or exceed the indexed revenue threshold. In this Order, we adopt our proposal and eliminate the difference between the application of the indexed revenue threshold for Part 32 and Part 64 cost allocation purposes. Carriers will be classified as Class A or Class B at the start of the calendar year following the first time their annual operating revenues equal or exceed the indexed revenue threshold.³⁸

18. The \$7 billion threshold will not be indexed for inflation annually, but instead will be a fixed threshold that the Commission will monitor on a regular basis. If we determine that the \$7 billion threshold is no longer appropriate due to inflation or any other change in market conditions, we will revise the threshold to reflect those changes.

B. Reduced Cost Allocation Manual Procedures for Mid-Sized ILECs

19. Section 64.903 of the Commission's rules requires ILECs with \$112 million or more in annual operating revenues to file CAMs setting forth the cost allocation procedures that they use to

³⁶ *Accounting Notice*, 13 FCC Rcd at 12975, ¶ 5.

³⁷ GTE Comments at 12; USTA Comments at 11. Ameritech observes that if we adopt Class B accounting for all carriers there would be no effect on the jurisdictional separations process. Ameritech Comments at 8.

³⁸ Although we sought comment on this issue, no commenters addressed it.

allocate costs between regulated and nonregulated services.³⁹ Carriers that are required to file CAMs are also required by section 64.904 to perform an independent audit of reported cost allocation data.⁴⁰

20. In the *Accounting Notice* we proposed to reduce CAM requirements for mid-sized ILECs.⁴¹ The proposal would allow these companies to submit their CAMs based upon the Class B system of accounts and would relax the current annual audit requirements for cost allocations related to the CAM by permitting mid-sized ILECs to obtain an attestation every two years.⁴² Each such attestation would cover the previous two years. Specifically, the proposed action would reduce the reporting requirements related to the nonregulated activity matrix and the cost apportionment section of the CAM. In addition, mid-sized ILECs would be subject to fewer audit reporting requirements and a significantly less stringent standard for testing, reporting, and expression of opinion than currently required.⁴³

21. The large ILECs contend that this proposal should be extended to all carriers;⁴⁴ other commenters support the proposal.⁴⁵ In section III. A above, we concluded that mid-sized ILECs may

³⁹ 47 C.F.R. § 64.903. These CAMs include the following: (a) a description of the company's nonregulated activities; (b) a list of the activities that the company accords incidental accounting treatment; (c) a chart showing all of its corporate affiliates; (d) a statement identifying affiliates that engage in or will engage in transactions with the carrier entity and describing the nature, terms, and frequency of such transactions; (e) detailed specifications for each USOA account and subaccount, of the cost categories to which amounts in the account or subaccount will be assigned and of the basis on which each cost category will be apportioned; and (f) a description of the carrier's time reporting procedures.

⁴⁰ The audit must provide a positive opinion that the reported data is presented fairly in all material respects and that the audit shall be conducted in accordance with generally accepted auditing standards, except as otherwise directed by the Chief, Common Carrier Bureau.

⁴¹ *Accounting Notice*, 13 FCC Rcd at 12980-81, ¶¶ 10-12.

⁴² In such an audit, the independent auditor expresses an opinion about whether the carriers' accounting and cost allocation procedures are in accordance with the Commission's rules.

⁴³ The current financial audit is a comprehensive examination requiring a positive opinion that the data shown in the carrier's ARMIS 43-03 report are fairly presented in accordance with the carrier's cost allocation manual and the Commission's rules. In an attest engagement, the independent auditor merely expresses an opinion that the carrier's accounting and cost methodologies are in accordance with the Commission's rules. Financial audits are considerably more expensive than attest audits because they require the auditor to express an opinion, not only on whether the methodologies are in compliance with our rules, but that the data are presented fairly. This requires more extensive audit work to substantiate the data.

⁴⁴ See, e.g., GTE Comments at 13-16; BellSouth Comments at 12; SBC Comments at 19-20; US West Comments at 8-10; Ameritech Comments at 10-11.

⁴⁵ See, e.g., Sprint Comments at 5-6; Comsat Comments at 1-2; CBT Comments at iii; ITTA Comments at 2.

maintain their accounts at the Class B level. Consistent with our change in the level of accounting detail required, we conclude that mid-sized ILECs may also submit their CAMs based upon the Class B system of accounts.⁴⁶ Allowing mid-sized ILECs to submit their CAMs based upon the Class B system of accounts reduces the reporting burden of the nonregulated activity matrix and the cost apportionment section of the CAM.⁴⁷ We also conclude that mid-sized ILECs only need to obtain an attestation every two years, that covers the prior two years. Such attestation would require significantly less stringent standards of testing, reporting, and expression of opinion than the present audit requirement. We reach these conclusions based on the reasoning supporting our decision to streamline the accounting requirements for mid-sized ILECs. Our experience with mid-sized ILECs leads us to conclude that we can maintain the necessary degree of oversight and monitoring to protect consumers' interests, while imposing less administratively burdensome requirements on such carriers.

22. Under the current Part 64 rules, carriers with operating revenues below the indexed revenue threshold (currently \$112 million in operating revenues) are not required to file a CAM or conduct external audits. USTA requests that we grant this status to all carriers that fall under the \$7 billion revenue threshold determining mid-sized ILEC status, and that we find that companies under the \$7 billion revenue threshold are not required to file CAMs or conduct external audits.⁴⁸ We do not find such treatment appropriate. We believe that obtaining Class B information will provide us with needed data. The requirement to file CAMs based on Class B accounts and obtain an attest audit every two years therefore applies to mid-sized ILECs with aggregate revenues below \$7 billion but equal to or above the indexed revenue threshold (*i.e.*, currently \$112 million). Thus, we are not imposing new requirements on carriers that are below the current indexed revenue threshold. Instead, we meet our objective to reduce the burdens on mid-sized ILECs by permitting certain carriers who would otherwise be required to file CAMs based on Class A accounts to file CAMs based on Class B accounts. For the large ILECs, we take no action at present but we direct the Common Carrier Bureau, as part of its comprehensive accounting review, to examine alternatives that will reduce the burden on large ILECs for undertaking annual CAMs while ensuring that the public interest is protected.

C. Independent Telephone and Telecommunications Alliance Petition for Forbearance

23. On February 17, 1998, ITTA filed a petition for forbearance requesting that the Commission forbear from applying to mid-sized ILECs, among other things, several reporting and recordkeeping requirements, including Class A accounting rules, CAM filings, audits, and detailed

⁴⁶ Carriers qualifying for this less burdensome treatment may, at their discretion, opt to prepare their CAM based on the Class A system of accounts.

⁴⁷ Class A carriers are required to provide cost allocation procedures for 178 of the Part 32 accounts. Class B carriers are required to provide cost allocation procedures for 55 accounts.

⁴⁸ USTA Comments at 13.

property records.⁴⁹ Two commenters, CBT and ATU, support the ITTA petition;⁵⁰ five commenters would have the relief sought by ITTA extended to all carriers.⁵¹ This Order will address ITTA's forbearance request regarding these financial reporting and recordkeeping requirements. The remaining issues raised in the ITTA petition will be addressed in other proceedings.⁵²

24. The ITTA petition is filed under section 10 of the Communications Act.⁵³ Specifically, section 10 provides that the Commission shall forbear from applying any regulation or any provision of the Communications Act to a telecommunications carrier or telecommunications service, or class of telecommunications carriers or telecommunications services, in any or some of its or their geographic markets, if the Commission determines that:

- (1) enforcement of such regulation or provision is not necessary to ensure that the charges, practices, classifications, or regulations by, for, or in connection with that telecommunications carrier or telecommunications service are just and reasonable and are not unjustly or unreasonably discriminatory;
- (2) enforcement of such regulation or provision is not necessary for the protection of consumers; and
- (3) forbearance from applying such provision or regulation is consistent with the public interest.⁵⁴

25. Class A accounting requirements. ITTA contends that we should not require Class A accounting requirements on mid-size LECs and that Class B accounting requirements should be

⁴⁹ Petition for Forbearance of the Independent Telephone and Telecommunications Alliance, filed February 17, 1998 (ITTA Petition). The deadline for the Commission's action on ITTA's petition was extended by 90 days to May 18, 1999. See Petition for Forbearance of the Independent Telephone and Telecommunications Alliance, ASD File No. 98-43, *Order*, 14 FCC Rcd 1018 (1999). Comments were filed by GTE Service Corporation (GTE), United States Telephone Association (USTA), the Telecommunications Resellers Association (TRA), General Communication, Inc. (GCI), Ameritech, SBC Communications, Inc. (SBC), AT&T, and Bell Atlantic. Reply Comments were filed by Cincinnati Bell Telephone Company (CBT), ITTA, and ATU Telecommunications (ATU).

⁵⁰ See CBT Reply Comments at 5-11; ATU Reply Comments at 2.

⁵¹ See Ameritech Comments at 2-4; SBC Comments at 1-2; Bell Atlantic Comments at 2-5; USTA Comments at 7-11; GTE Comments at 4-8.

⁵² See note 5 *supra*.

⁵³ 47 U.S.C. § 160.

⁵⁴ 47 U.S.C. § 160(a).

sufficient.⁵⁵ Essentially, ITTA is asking us to change our rules, not to forbear from applying the current rules. As discussed above, we are adopting the proposal in the *Accounting Notice* to streamline accounting requirements for mid-sized ILECs based on the aggregate revenues of the ILEC and any ILEC that it controls, is controlled by, or with which it is under common control.⁵⁶ If the aggregate revenues of these affiliated ILECs are less than \$7 billion, then each ILEC within that group will now be eligible for Class B accounting, even if the annual operating revenue of any individual ILEC equals or exceeds \$112 million. This rule change limits Class A accounting to the BOCs and GTE. All other ILECs, *i.e.*, the mid-size ILECs, may use the Class B system of accounts.⁵⁷ We are providing the relief sought by ITTA by permitting mid-sized ILECs to use Class B system of accounts. With this rule modification, there is no longer an accounting rule from which forbearance can be sought.⁵⁸ ITTA's petition for forbearance is therefore moot with respect to this issue.

26. CAM filings, audits, and property records. Section 64.903 of the Commission's rules requires ILECs with \$112 million or more in annual operating revenues to file CAMs setting forth the cost allocation procedures that they use to allocate costs between regulated and nonregulated services.⁵⁹ ITTA argues that the Commission should forbear from requiring mid-size ILECs (1) to file detailed CAMs; (2) to undergo annual audits; and (3) to maintain detailed property records under section 32.2000(e)-(f).⁶⁰ For the reasons set forth below, we conclude that ITTA has not demonstrated that the three requirements of section 10 have been satisfied and we deny the petition for forbearance.⁶¹

27. With respect to the first and second prongs of the section 10 standard for forbearance, we are not convinced by ITTA's assertion that compliance with Parts 64 and 32 of the Commission's rules can be adequately monitored through the tariff review and complaint process or through random audits.⁶² We cannot assume, based on ITTA's unsupported assertion, that the tariff review and complaint process and random audits will adequately ensure that charges, practices, classifications,

⁵⁵ ITTA Petition at 16.

⁵⁶ See 47 C.F.R. § 32.9000.

⁵⁷ Carriers that qualify for Class B accounting may, at their discretion, maintain a Class A accounting structure. See 47 C.F.R. § 32.11(d).

⁵⁸ ITTA observes that adoption of the modifications proposed in the *Accounting Notice* may moot some of the issues raised in the ITTA Petition. ITTA Comments at 6.

⁵⁹ 47 C.F.R. § 64.903.

⁶⁰ ITTA Petition at 14-15 & n.36.

⁶¹ AT&T and GCI argue that ITTA has failed to show that the elimination of these accounting safeguards meets the standards set forth in section 10(a) of the Communications Act. See AT&T Comments at 1-6; GCI Comments at 4-6.

⁶² See ITTA Petition at 16.

and services of the mid-sized ILECs are just and reasonable and are not unjustly or unreasonably discriminatory and that enforcement of these regulations is not necessary for the protection of consumers. ITTA has not brought such evidence to our attention. We fail to see how ITTA's proposal to eliminate reporting requirements that show how costs are allocated between regulated and nonregulated services would adequately protect consumers. Therefore, we conclude that the first and second prongs of the section 10 forbearance test have not been satisfied.

28. With respect to the third prong, we find that ITTA has not shown that any burden resulting from these reporting requirements and audits outweighs the public interest benefits. In evaluating whether forbearance is consistent with the public interest, we must "consider whether forbearance from enforcing the provision or regulation will promote competitive market conditions, including the extent to which forbearance will enhance competition among providers of telecommunications services."⁶³ We note that the mid-size LECs are dominant in their market areas.⁶⁴ We reject ITTA's contentions that the costs imposed by these regulations are disproportionate to their regulatory purpose and that these requirements are wholly unnecessary to curb anti-competitive pricing or to protect consumers.⁶⁵ The record does not show that eliminating CAMs, audits, and continuing property records will promote competitive market conditions or will enhance competition among local exchange providers. Neither does the record show that eliminating these reporting requirements will protect ratepayers and ensure that the mid-sized carriers' rates will be just, reasonable, and non-discriminatory. We believe that protecting ratepayers and ensuring that the mid-sized carriers' rates are just, reasonable, and non-discriminatory are significant elements of our public interest analysis. We therefore conclude that ITTA has not satisfied the third prong of the section 10 forbearance standard. For these reasons, we deny ITTA's petition for forbearance from CAM filing requirements, audit requirements, and detailed property record requirements.

29. In conclusion, we note that in this Order we are significantly streamlining accounting requirements for mid-sized ILECs. We are reducing our accounting requirements to permit mid-size LECs to use Class B system of accounts. Additionally, mid-sized ILECs are permitted to submit their CAMs based on the Class B system of accounts, thereby reducing the reporting burden of carriers subject to CAM requirements. We are also modifying our audit requirements, so that mid-sized ILECs will now only be required to obtain an attestation every two years, instead of an annual financial audit requiring a positive opinion. Finally, the Common Carrier Bureau has initiated a broad comprehensive review of all of our accounting and reporting requirements. Thus, a significant amount of the relief sought by ITTA in the Petition for Forbearance is realized through the rule changes adopted in this proceeding.

⁶³ 47 U.S.C. § 160(b).

⁶⁴ In its December 1998 report, the Industry Analysis Division concluded that for 1997, the most recent year for which data was available, the ILECs' share of nationwide local revenue was 97 percent, a decline of only three percent from 1993. See "Local Competition Report," Industry Analysis Division, Common Carrier Bureau (December 1998).

⁶⁵ ITTA Petition at 17-18.

D. Revising the Uniform System of Accounts for All Carriers

30. We have conducted a review of our USOA accounts and conclude that a number of accounts or filing requirements may be reduced or eliminated. A description of these changes and a discussion of our rationale for our conclusions are set forth below. These modifications will apply to all carriers subject to Part 32 of the Commission's rules.

31. *Combining Accounts 2114, 2115, and 2116.*⁶⁶ In the *Accounting Notice*, we proposed adopting USTA's recommendation that we combine Account 2114, Special purpose vehicles, Account 2115, Garage work equipment, and Account 2116, Other work equipment, into a single new account.⁶⁷ The assets recorded in these accounts are similar in nature, have similar prescribed depreciation rates,⁶⁸ and are treated identically under the jurisdictional separations rules set forth in Part 36 of our rules.⁶⁹ Commenters support this proposal.⁷⁰ We therefore conclude that these accounts should be combined into a single account entitled Account 2114, Tools and other work equipment, because combining these accounts would reduce the carriers' accounting and reporting burdens, would not affect the amounts separated between the interstate and intrastate jurisdictions, and would not affect our ability to protect the public interest.

32. *Combining Accounts 6114, 6115, and 6116.*⁷¹ In the *Accounting Notice*, we also proposed combining Account 6114, Special purpose vehicles expense, Account 6115, Garage work equipment expense, and Account 6116, Other work equipment expense, into a single new account entitled Account 6114, Tools and other work equipment expense.⁷² These accounts are similar in nature and are treated identically under the jurisdictional separations rules set forth in Part 36 of our rules.⁷³ Commenters support this proposal.⁷⁴ We conclude that these accounts should be combined

⁶⁶ 47 C.F.R. §§ 32.2114-32.2116.

⁶⁷ *Accounting Notice*, 13 FCC Rcd at 12981-82, ¶ 14 & n.34, citing letter dated February 19, 1998 from Porter E. Childers, USTA, to Kenneth P. Moran, FCC.

⁶⁸ See Simplification of the Depreciation Prescription Process, CC Docket No. 92-296, *Second Report and Order*, 9 FCC Rcd 3206, Appendix B (1994).

⁶⁹ 47 C.F.R. §§ 36.111, 36.112.

⁷⁰ See, e.g., SBC Comments at 25-26; USTA Comments at 20; ITTA Comments at 2; Lexcom Comments at 5; Comsat Comments at 1-2; Sprint Comments at 7; MCI Reply Comments at 12; PaPUC Reply Comments at 8.

⁷¹ 47 C.F.R. §§ 32.6114-32.6116.

⁷² See *Accounting Notice*, 13 FCC Rcd at 12982, ¶ 15.

⁷³ 47 C.F.R. §§ 36.111, 36.112.

⁷⁴ See, e.g., ITTA Comments at 2; Lexcom Comments at 5; Comsat Comments at 1-2; Sprint Comments at 7; Texas PUC Reply Comments at 7; PaPUC Reply Comments at 8.

into a single account because combining these accounts would reduce the carriers' accounting and reporting burdens, would not affect the amounts separated between the interstate and intrastate jurisdictions, and would not affect our ability to protect the public interest.

33. *Accounting for Nonregulated Revenues.* In the *Accounting Notice*, we proposed adopting USTA's request⁷⁵ that the Commission amend sections 32.23(c) and 32.5280 to allow carriers to record revenues from all nonregulated activities in Account 5280, Nonregulated operating revenue.⁷⁶ Such an amendment would modify the current rule that instructs carriers to record revenue from nonregulated activities in Account 5280 only if there is no other operating revenue account to which the revenue relates. USTA argues that the use of specific regulated accounts for individual nonregulated activities places carriers at a competitive disadvantage because competitors could determine product-specific revenue amounts related to ILECs' nonregulated products and services.⁷⁷ USTA also requests that the Commission eliminate Account 5010, Public telephone revenue.⁷⁸ ILECs record message revenue derived from public and semi-public telephone services provided within their basic service areas in account 5010. USTA argues that Account 5010 is no longer needed as a result of the deregulation of payphone services⁷⁹ as well as the changes it proposed with respect to Account 5280.⁸⁰

34. We conclude that the Commission's interest in protecting the public interest by ensuring that nonregulated revenues are segregated from the carriers' regulated revenues would continue to be served by allowing carriers to combine revenues for all nonregulated activities into one account.⁸¹ Thus, we grant USTA's petition, eliminating Account 5010 and revising the language in

⁷⁵ Petition for Rulemaking of the United States Telephone Association, filed Sept. 16, 1997 (USTA Petition). As noted in Appendix A, the comments filed in this proceeding were filed in CC Docket No. 98-81 and ASD File No. 98-64.

⁷⁶ 47 C.F.R. § 32.5280.

⁷⁷ See USTA Petition at 2. See also SBC Comments at 29-30; Ameritech Comments at 12; Lexcom Comments at 5; Sprint Comments at 7.

⁷⁸ USTA also requested a waiver of the rules to permit the accounting practice described above pending the outcome of its rulemaking petition. The waiver was granted on December 31, 1997. See United States Telephone Association Petition for Waiver of Part 32 of the Commission's Rules, AAD 97-103, *Order*, 13 FCC Rcd 214 (1997).

⁷⁹ Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996, CC Docket No. 96-128, *Report and Order*, 11 FCC Rcd 20541 (1996), *Order on Reconsideration*, 11 FCC Rcd 21233 (1996), *aff'd in part and remanded in part, sub nom. Illinois Public Telecommunications Ass'n v. FCC*, 117 F.3d 555 (D.C. Cir. 1997).

⁸⁰ See USTA Petition at 5.

⁸¹ In the order adopting section 32.5280, the Commission stated that it had no regulatory need for service-specific revenue data for nonregulated activities and that its regulatory objectives were satisfied by using a single account for this purpose. See Separation of Costs of Regulated Telephone Service from Costs of Nonregulated Activities, CC Docket No. 86-111, *Order on Further Reconsideration*, 3 FCC Rcd 6701, 6702-03, ¶ 13 (1988),

sections 32.23(c) and 32.5280(a), to require that all nonregulated revenues be recorded in Account 5280.⁸²

35. *Revision to Section 32.16, Changes in Accounting Standards.* Section 32.16 of the Commission's rules requires carriers to revise their records and accounts to reflect new accounting standards prescribed by the Financial Accounting Standards Board (FASB). This section provides that Commission approval of a change in an accounting standard shall automatically take effect 90 days after a carrier notifies the Commission of its intention to follow a new standard. In the notification to the Commission, carriers are required to provide a revenue requirement study that analyzes the effects of the accounting change for the current year and a projection for three years into the future.⁸³ In the *Accounting Notice*, we proposed to relieve carriers of the requirement to file the projected future effects of an accounting change in their notifications.⁸⁴ Several large ILECs argue that we should go beyond our proposal and allow price cap ILECs to adopt new accounting standards prescribed by the FASB without any requirement to notify, or obtain approval from the Commission.⁸⁵ MCI argues that the review process should be retained to assure uniformity in accounting practice.⁸⁶ After considering the comments, we have decided to adopt the proposal in the *Accounting Notice*. We conclude that we no longer need to receive projected effects of an accounting change routinely. Although this information was used in the past to assess the volatility of an accounting change over time, we have found that for most changes, an analysis of current effects is adequate to determine whether the change should be adopted. To the extent that projections are needed in the future, we can obtain them on an *ad hoc* basis as necessary. We do not adopt the ILECs' recommendation that price cap ILECs should be allowed to adopt new standards with no notification at all. Accounting standard changes often raise questions regarding exogenous treatment under price cap rules. When they do, cost data must be available to resolve such issues.

36. *Revision to Section 32.2000(b), Telecommunications Plant Acquired.* Section 32.2000(b)(4) of the Commission's rules requires carriers to submit for Commission approval the journal entries made to record acquisitions from other entities of telecommunications plant that cost

aff'd sub nom. Southwestern Bell Corp. v. FCC, 896 F.2d 1378 (D.C.Cir. 1990).

⁸² We note the concerns expressed by the PaPUC and the OCC on this matter. They argue that consolidating these accounts will, among other things, make it more difficult for regulators to determine whether carriers are engaged in anti-competitive behavior. See PaPUC Reply Comments at 9; OCC Reply Comments at 1. For federal purposes, we do not require this additional detail. States are free to require such detail for their purposes.

⁸³ 47 C.F.R. § 32.16(a).

⁸⁴ *Accounting Notice*, 13 FCC Rcd at 12983, ¶ 17.

⁸⁵ See, e.g., GTE Comments at 18; SBC Comments at 30; Ameritech Comments at 3; USTA Comments at 27.

⁸⁶ See MCI Reply Comments at 14.

more than \$1 million for Class A carriers and \$250,000 for Class B carriers.⁸⁷ In the *Accounting Notice*, we proposed to eliminate this filing requirement.⁸⁸ Commenters support our proposal.⁸⁹ We conclude that this requirement, which was established to ensure that plant acquired from other carriers is recorded at original cost as required in section 32.2000(b), is no longer necessary. The requirement to record plant acquired from other entities at original cost is well established, and we believe that other accounting safeguards such as ARMIS reporting and our audit program, together with our ability to obtain additional information as necessary, are sufficient to assure that carriers will comply with this accounting requirement. Accordingly, we adopt the proposal in the *Accounting Notice* and eliminate the requirement for routine filing of these journal entries.

E. Order on Reconsideration in CC Docket No. 96-150 – Section 274(f) Reporting Requirements

37. In the *Accounting Safeguards Order*, we addressed the accounting safeguards necessary to satisfy the requirements of sections 260 and 271 through 276 of the Communications Act, as amended by the 1996 Act.⁹⁰ Section 274(a) prohibits any "Bell operating company or any affiliate [from] engag[ing] in the provision of electronic publishing that is disseminated by means of such Bell operating company's or any of its affiliates' basic telephone service," other than through "a separated affiliate or electronic publishing joint venture."⁹¹ This separated affiliate or electronic publishing joint venture must, among other requirements, "maintain separate books, records, and accounts and prepare separate financial statements."⁹² Section 274(f) establishes a reporting requirement for separate electronic publishing affiliates created pursuant to section 274.⁹³ In the *Accounting Safeguards Order*, we concluded that in order to satisfy sections 274(b) and 254(k), we must apply our affiliate transactions rules, as modified in that order, to transactions between BOCs and their "separated" electronic publishing affiliates or joint ventures.⁹⁴ We concluded that our rules should require those section 274 affiliates that already file an SEC Form 10-K to file a copy with this

⁸⁷ 47 C.F.R. § 32.2000(b)(4).

⁸⁸ *Accounting Notice*, 13 FCC Rcd at 12983-84, ¶ 18.

⁸⁹ See, e.g., Sprint Comments at 7; Lexcom Comments at 5.

⁹⁰ Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (1996 Act). The 1996 Act amended the Communications Act of 1934.

⁹¹ 47 U.S.C. § 274(a).

⁹² 47 U.S.C. § 274(b)(1).

⁹³ 47 U.S.C. § 274(f).

⁹⁴ *Accounting Safeguards Order*, 11 FCC Rcd at 17638-39, ¶ 218.

Commission.⁹⁵ For those section 274 affiliates that were not required to file a Form 10-K with the SEC, we required them to file an identical form with us.⁹⁶

38. SBC Communications, Inc. (SBC) filed a Petition for Reconsideration⁹⁷ of the *Accounting Safeguards Order* asserting, among other things, that a simplified report for "separated entities" not already subject to the SEC's Form 10-K requirements will satisfy the intent of section 274(f) because the phrase "substantially equivalent," as used in the statute, does not mean "identical."⁹⁸ In addition, SBC recommended that the Commission accept unaudited financial statements that contain substantially the same financial information as the audited financial statements required by Item 8 of Form 10-K.⁹⁹ BellSouth asserted that, because the SEC has adopted reduced reporting requirements for wholly owned companies, the Commission should omit certain items from the section 274(f) Form 10-K filing requirement.¹⁰⁰ None of the parties specifically opposed SBC's petition. Cox, however, argued in its petition that our accounting rules do not provide interested parties with the data necessary to detect cross-subsidization.¹⁰¹

39. In this Order, we grant SBC's petition in part and deny it in part. We agree that the reporting requirements can be streamlined for those entities that are not required by the SEC to file a Form 10-K, but we decline to adopt SBC's proposal to submit unaudited information in its substantially equivalent form. Audited data provides a level of assurance that the company's internal controls are in place and functioning. In light of the private right of action permitted under section 274(e), third parties require assurances of the reliability and accuracy of the information reported in the Form 10-K. Failure to require audited data could potentially undermine the analysis conducted by a third party to ascertain the existence of anti-competitive conduct.

40. The SEC Form 10-K is a voluminous report that contains a description of the company filing the report and its operations, financial statements with supporting financial data and

⁹⁵ *Id.* at 17645, ¶ 230.

⁹⁶ *Id.*

⁹⁷ Petition for Reconsideration of SBC Communications, Inc., filed Feb. 20, 1997 ("SBC Petition"). Petitions for reconsideration on other issues were filed by Ameritech, GTE, American Public Communications Council, Cincinnati Bell Telephone Company, Southern New England Telephone Company, MCI Telecommunications Corporation, and Cox Communications, Inc. The SBC Petition also addressed other issues. This order is limited to the section 274 issue. The remaining issues will be addressed in another Order on Reconsideration.

⁹⁸ SBC Petition at 16. The following comments or responses were filed in CC Docket No. 96-150 supporting SBC's argument: Ameritech Comments at 5-6; BellSouth Comments at 6-7; US West Comments at 6; Bell Atlantic/NYNEX Comments at 6.

⁹⁹ SBC Petition at 17. *See also* Ameritech Comments at 6; US West Comments at 6.

¹⁰⁰ BellSouth Comments at 6-7.

¹⁰¹ *See* Cox Petition at 6-9.

major legal and financial disclosures concerning the company. The SEC Form 10-K is comprised of the following items: Item 1, Business; Item 2, Properties; Item 3, Legal Proceedings; Item 4, Submission of Matters to a Vote of Security Holders; Item 5, Market for Registrant's Common Equity and Related Stockholder Matters; Item 6, Selected Financial Data; Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations; Item 8, Financial Statements and Supplementary Data; Item 9, Changes in and Disagreements with Accountants on Accounting and Financial Disclosure; Item 10, Directors and Executive Officers of the Registrant; Item 11, Executive Compensation; Item 12, Security Ownership of Certain Beneficial Owners and Management; Item 13, Certain Relationships and Related Transactions; and Item 14, Exhibits, Financial Statement Schedules and Reports on Form 8-K. The SEC also has a limited version of the Form 10-K for wholly owned subsidiaries. The limited version omits Items 4, 10, 11, 12, and 13, which are items that generally address issues related to investor information. The limited version also streamlines Items 6 and 7, which require data spanning a five-year period.

41. We conclude that the information contained in the limited version of SEC Form 10-K, with certain modifications, will enable the Commission to monitor the electronic publishing affiliate's compliance with the section 274 requirements. We modify the limited Form 10-K filing requirements to exclude Item 5 and include Item 10. Item 5 is related to stockholder matters that are not relevant to section 274. We retain Item 10 for section 274 affiliates because Item 10 contains information on directors and officers that would assist the Commission in monitoring the prohibition against sharing directors and officers. We find that these modifications will ensure that BOCs disclose key information about their electronic publishing affiliates in a manner that both satisfies the section 274(f) disclosure requirements and reduces their reporting burden.

F. Accounting for Computer Software Costs

42. *Generally accepted accounting principles (GAAP).* Since 1985, the Commission has followed a policy of conforming regulatory accounting for carriers to GAAP, including new FASB standards, unless the principle or practice conflicts with the Commission's regulatory objectives.¹⁰² Accordingly, several parties have taken the Commission up on its request for the submission of additional proposals for accounting changes by suggesting the adoption of GAAP accounting in lieu of current Commission accounting for various purposes.¹⁰³ While a wholesale replacement of our accounting rules with GAAP is not warranted at this time as requested by some parties -- such issues will be considered as part of the Common Carrier Bureau's recently initiated comprehensive accounting review -- we do change our accounting rules relating to the use of GAAP in one respect in this order.

¹⁰² See RAO Letter 20 Concerning Uniform Accounting for Postretirement Benefits Other Than Pensions, *et al.*, 12 FCC Rcd 2321, (1997), citing Revision of Uniform System of Accounts for Telephone Companies to Accommodate Generally Accepted Accounting Principles, 102 FCC 2d 964 (1985).

¹⁰³ See, e.g., Bell Atlantic Comments at 7-9; BellSouth Comments at 20-21; SBC Comments at 3; Ameritech Comments at 8; US West Comments at 4-7; GTE Comments at 18-19; USTA Comments at 3, 21-25; ALLTEL Comments at 4. Some commenters opposed the use of GAAP in lieu of Commission accounting rules. See, e.g., Oklahoma Corporation Commission Reply Comments; Ohio PUC Reply Comments at 2-14.

43. Specifically, when the Commission adopted the uniform system of accounts, we required that the original cost of operating system software be recorded in the same account as the associated plant rather than a separate software account.¹⁰⁴ The Commission further required that the cost of subsequent additions and modifications be expensed barring exceptional circumstances.¹⁰⁵ Later, the Commission clarified the requirements relating to software costs by directing that the cost of all software not considered initial operating system software (*i.e.*, application software) be recorded in conformance with GAAP, which could result in the expensing or capitalization of such software costs depending on the circumstances.¹⁰⁶

44. In a related matter concerning GAAP, on March 4, 1998, the American Institute of Certified Public Accountants issued Statement of Position 98-1 ("SOP 98-1") to provide authoritative guidance on accounting for the costs of computer software effective for financial statements for fiscal years beginning after December 15, 1998.¹⁰⁷ SOP 98-1 generally requires the capitalization of software costs.¹⁰⁸ SOP 98-1 also requires the cost of upgrades and enhancements to be capitalized if they result in additional functionality.¹⁰⁹

45. On August 3, 1998, Bell Atlantic and BellSouth ("Joint Petitioners") filed a petition for rulemaking to amend the Commission's existing Part 32 rules in order to accommodate recent changes in GAAP.¹¹⁰ The Joint Petitioners request that the Commission change its rules governing

¹⁰⁴ See Revision of the Uniform System of Accounts and Financial Reporting Requirements for Class A and Class B Telephone Companies (Parts 31, 33, 42, and 43 of the FCC's Rules), CC Docket No. 78-196, *Report and Order*, 60 Rad. Reg. 2d (P&F) 1111 (1986) at ¶ 132; 47 C.F.R. 32.2000(i). The Commission believed that this struck a balance between capitalization and expensing that was (a) more consistent with current industry practice, (b) reduced difficulties associated with segregations of costs and identifying periods of benefit when classifying software, and (c) gave greater weight to consideration of individual circumstances.

¹⁰⁵ *Id.*

¹⁰⁶ Responsible Accounting Officer Letter No. 7 (RAO 7), *Part 32, Uniform System of Accounts for Class A and Class B Carriers—Questions and Answers* (Issued July 7, 1987) at 4.

¹⁰⁷ American Institute of Certified Public Accountants (AICPA) Statement of Position 98-1, *Accounting for the Costs of Computer Software Developed or Obtained for Internal Use*, Issued by the Accounting Standards Executive Committee, March 4, 1998, at Summary.

¹⁰⁸ *Id.* at 5. SOP 98-1 requires that "once the capitalization criteria of the SOP have been met, external direct costs of materials and services consumed in developing or obtaining internal-use computer software...should be capitalized." *Id.*

¹⁰⁹ *Id.*

¹¹⁰ Petition for Rulemaking to Amend Part 32 of the Commission's Rules, *Uniform System of Accounts for Class A and Class B Telephone Companies, to Adopt the Accounting for Software Required by Statement of Position 98-1*, filed August 3, 1998 ("Petition"). On August 13, 1998, the Commission released a Public Notice seeking comment on the petition. "BellSouth and Bell Atlantic File a Petition for Rulemaking to Amend Part 32 of the Commission's Rules to Adopt the Accounting for Software Required by Statement of Position 98-1,"

the treatment of software costs to conform with SOP 98-1.¹¹¹ Joint Petitioners request that capitalized software costs be classified as an intangible asset to Account 2690, Intangibles.¹¹² Joint Petitioners also seek a waiver of the requirement to provide a revenue requirement study under section 32.16, Changes in accounting standards,¹¹³ of the Commission's rules.¹¹⁴

46. All commenters, except MCI, agree with Joint Petitioners that software meets the definition of an intangible asset and that capitalized computer software costs should be treated as an intangible asset in Account 2690, Intangibles.¹¹⁵ Joint Petitioners argue that their Petition seeks to avoid the inconsistency associated with the separate treatment of application and operating system software, which have the same physical properties and cannot be differentiated except for the type of program instructions the computer uses to perform its tasks.¹¹⁶ MCI, on the other hand, contends that the Commission should continue to require the treatment of operating system software as a tangible asset, capitalized to the same account as the associated hardware, and depreciated over the economic useful life of the plant.¹¹⁷ MCI claims that intangible treatment of operating system software would severely complicate both cost accounting and service cost studies as well as increase the possibilities of inaccurate or improper cost allocations.¹¹⁸

47. We conclude that the facts and circumstances differ in each situation regarding types of software, and thus, it would not be appropriate to adopt a rule strictly requiring all software costs to be capitalized to a plant account or an intangible account. Instead, we find that SOP 98-1 and

Public Notice, RM-9341, 13 FCC Rcd 15524 (1998). Six parties submitted comments ("RM-9341 Comments"): MCI Telecommunications Corporation (MCI); Cincinnati Bell Telephone (CBT); GTE Services Corporation (GTE); Ameritech; United States Telephone Association (USTA); Southwestern Bell Telephone Company, Pacific Bell, and Nevada Bell (collectively, SBC). Five parties submitted reply comments ("RM-9341 Reply Comments"): Joint Petitioners; MCI WorldCom; GTE; Ameritech; SBC. All of the foregoing parties also filed comments or reply comments in this proceeding (CC Docket No. 98-81).

¹¹¹ Petition at 2.

¹¹² *Id.* at 4.

¹¹³ 47 C.F.R. § 32.16.

¹¹⁴ Petition at 6. Joint Petitioners claim that good cause exists for the grant of a waiver because the Commission has modified the price cap rules to exclude exogenous treatment for accounting changes that have no cash flow impact. Therefore, because the accounting change has no impact on rates, a revenue requirement study would serve no useful purpose. *Id.*

¹¹⁵ See, e.g., Petition at 4-5; Ameritech RM-9341 Comments at 2; CBT RM-9341 Comments at 3-4; GTE RM-9341 Comments at 3-6; USTA RM-9341 Comments at 2.

¹¹⁶ See Joint Petitioner's Reply Comments at 2.

¹¹⁷ MCI RM-9341 Comments at 3-4.

¹¹⁸ *Id.*

current authoritative accounting guidance (*i.e.*, GAAP) are sufficient to determine whether capitalizable software costs should be treated as an intangible asset recorded in the intangible asset account or treated as a tangible asset classified to the same account as the associated hardware.¹¹⁹ Accordingly, all carriers must account for computer software costs in accordance with GAAP.¹²⁰

48. *Amortization.* Commenters agree with Joint Petitioners that there is no need for the Commission to define specific amortization periods for software capitalized to the intangible asset account.¹²¹ Commenters recommend that amortization periods be determined by each company based on the estimated useful life of the software at the time it is placed into service consistent with GAAP.¹²² We agree with this position. We believe that GAAP and the Commission's rules concerning amortization accounting provide adequate guidance to ensure accurate and reliable cost information. Therefore, we do not elect to set amortization periods or amortization period ranges for software in this order. We expect, however, that amortization periods based on GAAP adopted for regulatory purposes will not be less than amortization periods used for external financial reporting purposes. We require any carrier wishing to adopt software amortization periods for regulatory purposes that are less than amortization periods used for external reporting purposes to obtain prior Commission approval.

49. In order to monitor the recording and reporting of capitalizable software costs in the intangible asset account for regulatory purposes, we require that carriers establish and maintain subsidiary record categories for general purpose computer ("GPC") software and network software within the intangible asset account. The cost of software upgrades and enhancements will continue to be expensed or capitalized in accordance with GAAP.¹²³ We will also allow non-price cap carriers to capitalize software upgrades and enhancements that may cause large one-time expense "spikes"

¹¹⁹ The Accounting Standards Executive Committee, the senior technical body of the AICPA, decided that it was not necessary to characterize computer software as either intangible assets or tangible assets when similar characteristics have not been made for most other assets. See SOP 98-1, p. 28, ¶ 65.

¹²⁰ See 47 C.F.R. § 32.12(a).

¹²¹ See, *e.g.*, Joint Petitioner's RM-9341 Reply Comments at 4-6; Ameritech RM-9341 Comments at 2-3; CBT RM-9341 Comments at 4-6; GTE RM-9341 Comments at 6-7; SBC RM-9341 Comments at 3; USTA RM-9341 Comments at 2-3.

¹²² CBT argues that the Commission should either not prescribe amortization periods at all or should adopt the ranges suggested in CBT's Comments (1 to 3 years for network based software and 2 to 5 years for general and administrative software). See CBT RM-9341 Comments at 4.

¹²³ The term "upgrades and enhancements" as used in this order and SOP 98-1 is synonymous with the term "subsequent additions and modifications" referred to and addressed in CC Docket 78-196.

regardless of whether such upgrades or enhancements result in additional functionality required for capitalization under SOP 98-1.¹²⁴

50. *Expense limit requirement.* As a result of the changes we are making in this Order – adopting GAAP treatment for all computer software costs – we must address the expense limit requirements for general purpose computers in section 32.2000(a)(4)¹²⁵ of the Commission's rules. In the *Expense Limit Order*, the Commission specifically retained the \$500 expense limit for personal computers falling within Account 2124, General purpose computers, that includes the cost of operating system software.¹²⁶ In this Order, however, we eliminate the distinction between application and operating system software and adopt GAAP for the recording of computer software costs in Part 32. As a result, the cost of operating system software, classifiable to Account 2690, will no longer be recorded in Account 2124. Therefore, we must modify our rules to exclude the cost of operating system software from the \$500 expense limit for personal computers falling within Account 2124.

51. *Other issues.* We do not address Joint Petitioners' request for a waiver of the revenue requirement study because our action in this Order renders this request moot. A revenue requirement study is irrelevant and would serve no useful purpose because we are amending our rules to adopt the new accounting guidance in SOP 98-1. Similarly, we do not address exogenous treatment of the accounting change. We note that Joint Petitioners and all commenting parties agree that the accounting change does not necessitate an exogenous price cap adjustment because it does not affect a carrier's cash flow, only the timing of the recovery of costs.¹²⁷

IV. CONCLUSION

52. In this Order, we streamline the accounting requirements for mid-sized ILECs whose aggregate revenues are less than \$7 billion. We also conclude that mid-sized ILECs should be permitted to submit their CAMs based on the Class B system of accounts, thereby reducing the reporting burden of carriers subject to CAM requirements. Mid-sized ILECs will now only be required to obtain an attestation every two years, instead of an annual financial audit requiring a positive opinion. For all carriers subject to our accounting rules, we reduce or eliminate a number of accounting requirements that are no longer necessary. In addition, we modify our holding in the

¹²⁴ See Revision of the Uniform System of Accounts and Financial Reporting Requirements for Class A and Class B Telephone Companies (Parts 31, 33, 42, and 43 of the FCC's Rules), CC Docket No. 78-196, *Report and Order*, 60 Rad. Reg. 2d (P&F) 1111 (1986) at ¶ 132; Chouteau Telephone Company, *et al.*, RM-6911, *Memorandum Opinion and Order*, 5 FCC Rcd 2795, 2796-97, ¶ 13 (1990).

¹²⁵ 47 C.F.R. § 32.2000(a)(4).

¹²⁶ Revision to Amend Part 32, Uniform System of Accounts for Class A and Class B Telephone Companies to Raise the Expense Limit for Certain Items of Equipment from \$500 to \$750, CC Docket No. 95-60, *Report and Order*, 12 FCC Rcd 7566, 7572, ¶ 10 (1997) (*Expense Limit Order*).

¹²⁷ See, e.g., SBC RM-9341 Comments at 4; USTA RM-9341 Comments at 3; GTE RM-9341 Comments at 8; Ameritech RM-9341 Comments at 3; MCI RM-9341 Comments at 7.

Accounting Safeguards Order and conclude that the information contained in the limited version of the SEC Form 10-K, with certain modifications, is sufficient to enable the Commission to monitor electronic publishing affiliates' compliance with the section 274 requirements. We deny ITTA's petition for forbearance on the issue that the Commission forbear from applying to mid-sized ILECs several reporting and recordkeeping requirements, including Class A accounting rules, CAM filings, audits, and detailed property records. We also amend our requirements regarding the accounting for computer software costs: the cost of all software must be recorded in conformance with GAAP. Finally, we recognize that our accounting and cost allocation rules need to be streamlined, and, as announced recently, the Common Carrier Bureau has initiated a comprehensive review of our accounting and reporting requirements.

V. PROCEDURAL ISSUES

A. Regulatory Flexibility Analysis

1. Final Regulatory Flexibility Certification – Report and Order in CC Docket No. 98-81, RM-9341

53. The Regulatory Flexibility Act (RFA)¹²⁸ requires that an agency prepare a regulatory flexibility analysis for notice-and-comment rulemaking proceedings, unless the agency certifies that "the rule will not, if promulgated, have a significant economic impact on a substantial number of small entities."¹²⁹ In the *Accounting Notice*,¹³⁰ the Commission certified that the proposed rules would not have a significant economic impact on a substantial number of small entities because such rules would reduce certain reporting requirements for mid-sized incumbent local exchange carriers (ILECs) and the changes would be easy and inexpensive for mid-sized ILECs to implement.¹³¹ No comments

¹²⁸ The RFA, 5 U.S.C. § 601 *et seq.*, has been amended by the Contract With America Advancement Act of 1996, Pub. L. No. 104-121, 110 Stat. 847 (1996) (CWAAA). Title II of the CWAAA is the Small Business Regulatory Enforcement Act of 1996 (SBREFA).

¹²⁹ 5 U.S.C. § 605(b).

¹³⁰ 1998 Biennial Regulatory Review -- Review of Accounting and Cost Allocation Requirements, CC Docket No. 98-81, *Notice of Proposed Rulemaking*, 13 FCC Red 12973 (1998).

¹³¹ With respect to the Petition for Rulemaking filed by Bell Atlantic and BellSouth to amend the Commission's existing Part 32 rules in order to accommodate recent changes in generally accepted accounting principles (GAAP), *see* Petition for Rulemaking to Amend Part 32 of the Commission's Rules, Uniform System of Accounts for Class A and Class B Telephone Companies, to Adopt the Accounting for Software Required by Statement of Position 98-1, filed August 3, 1998, the Commission concluded in the Report and Order that the facts and circumstances differ in each situation regarding types of software, thus it would not be appropriate to adopt a rule strictly requiring all software costs to be capitalized to a plant account or an intangible account. Instead, the Commission required that all carriers must account for computer software costs in accordance with GAAP. *See* 47 C.F.R. § 32.12(a), requiring financial records to be "kept in accordance with generally accepted accounting principles to the extent permitted by this system of accounts." This rule modification does not impose any additional compliance burden on small entities.

were received concerning this certification. The Commission now reaffirms this certification with respect to the rules adopted in this Report and Order. The Commission anticipates that the rule changes adopted here will reduce regulatory and procedural burdens on small entities. The rule modifications do not impose any additional compliance burden on persons dealing with the Commission, including small entities. Accordingly, the Commission certifies, pursuant to section 605(b) of the RFA, that the rules adopted herein will not have a significant economic impact on a substantial number of small business entities, as defined by the RFA.

2. Supplemental Final Regulatory Flexibility Analysis – Order on Reconsideration in CC Docket No. 96-150

54. As required by the Regulatory Flexibility Act (RFA), as amended,¹³² an Initial Regulatory Flexibility Analysis (IRFA) was incorporated in the *Notice of Proposed Rulemaking*¹³³ and a Final Regulatory Flexibility Analysis (FRFA) was incorporated into the *Report and Order* in CC Docket No. 96-150.¹³⁴

55. In the RFA, the Commission certified that the rules adopted in the Report and Order would not have a significant economic impact on a substantial number of small entities.¹³⁵ For the reasons stated below, the Commission certifies that the rule adopted herein in this Order on Reconsideration will not have a significant economic impact on a substantial number of small entities. This Supplemental Final Regulatory Flexibility Analysis (Supplemental FRFA) conforms to the RFA, as amended by the Small Business Regulatory Enforcement Fairness Act of 1996 (SBREFA).¹³⁶

56. Need for, and Objectives of, this Order on Reconsideration: In this Order on Reconsideration the Commission grants, in part, a petition for reconsideration regarding filing a "substantially equivalent" report for electronic publishing affiliates not already subject to Security and Exchange Commission (SEC) Form 10-K requirements. The Commission finds that the reporting requirements can be streamlined for such entities, and concludes that the information contained in the limited version of SEC Form 10-K, with certain modifications, will enable monitoring of electronic publishing affiliate's compliance with section 274 of the Communications Act. The Commission therefore permits the limited SEC Form 10-K, with the exclusion of Item 5 and inclusion of Item 10, to satisfy the section 274 requirements for electronic publishing affiliates not already subject to SEC Form 10-K requirements.

¹³² See 47 U.S.C. § 603.

¹³³ See Accounting Safeguards Under the Telecommunications Act of 1996, CC Docket No. 96-112, *Notice of Proposed Rulemaking*, 11 FCC Rcd 9054 (1996).

¹³⁴ See Accounting Safeguards Under the Telecommunications Act of 1996, CC Docket No. 96-150, *Report and Order*, 11 FCC Rcd 17539 (1996).

¹³⁵ 5 U.S.C. § 605(b).

¹³⁶ 5 U.S.C. §§ 601-611. SBREFA was enacted a Subtitle II of the Contract with America Advancement Act of 1996 (CWAAA), Pub. L. No. 104-121, 110 Stat. 847 (1996).

57. Summary of Significant Issues Raised by Reconsideration Petitions. No petitions were received in direct response to the FRFA in the *Report and Order*, nor were small business issues raised.

58. Description and Estimate of the Number of Small Entities to which the Rules Will Apply. The RFA generally defines "small entity" as having the same meaning as the terms "small business," "small organization," and "small governmental jurisdiction."¹³⁷ In addition, the term "small business" has the same meaning as the term "small business concern" under the Small Business Act.¹³⁸ A small business concern is one which: (1) is independently owned and operated; (2) is not dominant in its field of operation; and (3) satisfies any additional criteria established by the Small Business Administration (SBA).¹³⁹ Section 121.201 of the SBA regulations defines a small telecommunications entity in SIC code 4812 (Telephone Companies Except Radio Telephone) as any entity with 1,500 or fewer employees at the holding company level.¹⁴⁰ As explained below, the terms "small entities" and "small businesses" do not encompass the Bell operating companies (BOCs), the parties affected by this Order in Reconsideration.

59. As noted in the associated Final Regulatory Flexibility Certification in CC Docket No. 96-150, the RFA directs agencies to provide a Regulatory Flexibility Analysis in notice-and-comment rulemaking proceedings, unless the agency certifies that "the rule will not, if promulgated, have a significant economic impact on a substantial number of small entities." The Commission's action on reconsideration in CC Docket No. 96-150 affects only BOCs' affiliate entities engaged in electronic publishing. These rules do not apply to small entities because all entities subject to this rule are BOCs or entities associated or affiliated with BOCs. None of the BOCs is a small entity, since each BOC is an affiliate of a Regional Holding Company (RHC), and all the BOCs or their RHCs have more than 1,500 employees. Moreover, the entities affected by this rule that are associated or affiliated with the BOCs are not independently owned and operated, and therefore do not meet the definition of small entities. The Commission therefore certifies that the SEC Form 10-K filing requirement adopted in this Order on Reconsideration will not have a significant economic impact on a substantial number of small entities.

60. Description of Projected Reporting, Recordkeeping, and Other Compliance Requirements. As discussed above, in this Order on Reconsideration the Commission concludes that the information contained in the limited version of SEC Form 10-K, with the exclusion of Item 5 and

¹³⁷ 5 U.S.C. § 601(6).

¹³⁸ 5 U.S.C. § 601(3) (incorporating by reference the definition of "small business concern" in Small Business Act, 15 U.S.C. § 632). Pursuant to 5 U.S.C. § 601(3), the statutory definition of a small business applies "unless an agency, after consultation with the Office of Advocacy of the Small Business Administration and after opportunity for public comment, establishes one or more definitions of such term which are appropriate to the activities of the agency and publishes such definition(s) in the Federal Register."

¹³⁹ Small Business Act, 15 U.S.C. § 632.

¹⁴⁰ 13 C.F.R. § 121.201.

inclusion of Item 10, will satisfy the section 274 requirements for electronic publishing affiliates not already subject to SEC Form 10-K requirements. This reduces the reporting burden for BOC affiliates while providing sufficient information to the Commission to satisfy section 274 of the Communications Act.

61. Report to Congress. The Office of Public Affairs, Reference Operations Division, shall provide a copy of this certification and Supplemental Final Regulatory Flexibility Analysis to the Chief Counsel for Advocacy of the SBA, and include it in the report to Congress pursuant to the SBREFA.¹⁴¹ The certification and Supplemental Final Regulatory Flexibility Analysis will also be published in the Federal Register.¹⁴²

B. Final Paperwork Reduction Act Analysis

62. The decision herein, in CC Docket No. 98-81 and ASD File No. 98-64, has been analyzed with respect to the Paperwork Reduction Act of 1995, Pub. L. 104-13, and has been approved in accordance with the provisions of that Act. The Office of Management and Budget (OMB) approved the requirements under OMB control number 3060-0847 which expires October 31, 2001.

VI. ORDERING CLAUSES

63. Accordingly, IT IS ORDERED that, pursuant to Sections 1, 2, 4, 11, 201-205, and 218-220 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151, 152, 154, 161, 201-205, and 218-220, Parts 32 and 64 of the Commission's rules, 47 C.F.R. Parts 32 and 64, is AMENDED, as shown in Appendix B below.

64. IT IS FURTHER ORDERED that, pursuant to Section 220(g) of the Communications Act of 1934, as amended, 47 U.S.C. § 220(g), changes to our Part 32, System of Accounts, adopted in this Order shall take effect six months after publication in the Federal Register. We will, however, permit carriers to implement changes with respect to accounting for computer software costs, discussed in Section III. F., *supra*, as of January 1, 1999.

65. IT IS FURTHER ORDERED that, pursuant to Sections 1, 4, and 220 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151, 154, and 220, and Section 1.401 of the Commission's rules, 47 C.F.R. § 1.401, the Petition for Rulemaking of the United States Telephone Association is GRANTED to the extent indicated herein.

66. IT IS FURTHER ORDERED that, pursuant to Sections 1, 4, and 220 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151, 154, and 220, and Section 1.401 of the Commission's rules, 47 C.F.R. § 1.401, the Petition for Reconsideration of the *Accounting Safeguards Order* of SBC Communications, Inc. is GRANTED in part and DENIED in part. The

¹⁴¹ See 5 U.S.C. § 801(a)(1)(A).

¹⁴² See 5 U.S.C. § 605(b).

requirements and regulations adopted with respect to changes to section 274(f) reporting requirements shall become effective upon approval by OMB of the new information collection requirements adopted herein, but no sooner than 30 days after date of publication in the Federal Register.

67. IT IS FURTHER ORDERED that, pursuant to Sections 1, 4, and 220 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151, 154, and 220, and Section 1.401 of the Commission's rules, 47 C.F.R. § 1.401, the Independent Telephone and Telecommunications Alliance Petition for Forbearance is DISMISSED in part and DENIED in part to the extent indicated herein.

68. IT IS FURTHER ORDERED that, pursuant to Sections 1, 4, and 220 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151, 154, and 220, and Section 1.401 of the Commission's rules, 47 C.F.R. § 1.401, the Petition for Rulemaking of Bell Atlantic and BellSouth is GRANTED in part, to the extent indicated herein, and DENIED in part.

69. IT IS FURTHER ORDERED that the Commission's Office of Public Affairs, Reference Operations Division, shall send a copy of this Report and Order, including the Final Regulatory Flexibility Certification and Supplemental Final Regulatory Flexibility Analysis, to the Chief Counsel for Advocacy of the Small Business Administration.¹⁴³

FEDERAL COMMUNICATIONS COMMISSION



Magalie Roman Salas
Secretary

¹⁴³ See 5 U.S.C. § 605(b).

APPENDIX A**Parties Filing Comments and Reply Comments
(in CC Docket No. 98-81 and ASD File No. 98-64)****Parties Filing Comments**

ALLTEL Communications Service Corporation (ALLTEL)
Ameritech
AT&T Corporation (filed in ASD File No. 98-64 only)
Bell Atlantic Telephone Companies (Bell Atlantic)
BellSouth Corporation and BellSouth Telecommunications, Inc. (BellSouth)
Cincinnati Bell Telephone Company (CBT)
COMSAT Mobile Communications (COMSAT)
GTE Service Corporation (GTE)
Frontier Telephone of Rochester, Inc. (Frontier)
Independent Telephone & Telecommunications Alliance (ITTA)
Lexcom Telephone Company (Lexcom)
MCI Telecommunications Corporation (MCI)
Southwestern Bell Telephone Company, Pacific Bell, and Nevada Bell (SBC)
Sprint Local Telephone Companies (Sprint)
US West, Inc.
United States Telephone Association (USTA)

Parties Filing Reply Comments

ALLTEL
Ameritech
AT&T
Bell Atlantic
BellSouth
Florida Public Service Commission (Florida PSC)
General Services Administration (GSA)
GTE
MCI
Oklahoma Corporation Commission (OCC)
Pennsylvania Public Utility Commission (PaPUC)
Public Service Commission of Wisconsin (PSCW)
Public Utility Commission of Ohio (PUCO)
Public Utility Commission of Texas (Texas PUC)
State Members of the Joint Board in CC Docket No. 80-286
US West, Inc.
USTA

APPENDIX B – FINAL RULES

Part 32 of Title 47 of the C.F.R. is amended as follows:

PART 32 - UNIFORM SYSTEM OF ACCOUNTS FOR TELECOMMUNICATIONS COMPANIES

1. The authority citation for Part 32 continues to read as follows:

Authority: 47 U.S.C. 154(i), 154(j) and 220 as amended, unless otherwise noted.

2. Table of Contents, Part 32-Uniform System of Accounts for Telecommunications Companies, Subpart C - Instructions for Balance Sheet Accounts is revised to rename 32.2114 Special purpose vehicles to 32.2114 Tools and other work equipment and to delete 32.2115 Garage work equipment, and 32.2116 Other work equipment.

3. Table of Contents, Part 32-Uniform System of Accounts for Telecommunications Companies, Subpart D - Instructions for Revenue Accounts is revised to delete 32.5010 Public telephone revenue.

4. Table of Contents, Part 32-Uniform System of Accounts for Telecommunications Companies, Subpart E - Instructions for Expense Accounts is revised to rename 32.6114 Special purpose vehicles expense to 32.6114 Tools and other work equipment expense and to delete 32.6115 Garage work equipment expense and 32.6116 Other work equipment expense.

5. Section 32.11 Classification of companies is amended by revising paragraphs (b), (c), (d), and (e) to read as follows:

§ 32.11 Classification of companies.

* * * * *

(b) Class A companies, except mid-sized incumbent local exchange carriers, as defined by § 32.9000, shall keep all the accounts of this system of accounts which are applicable to their affairs and are designated as Class A accounts. Class A companies which include mid-sized incumbent local exchange carriers shall keep Basic Property Records in compliance with the requirements of §§ 32.2000(e) and (f) of subpart C.

(c) Class B companies shall keep all accounts of this system of accounts which are applicable to their affairs and are designated as Class B accounts. Class B companies shall keep Continuing Property Records in compliance with the requirements of §§ 32.2000(e)(7)(A) and 32.2000(f) of subpart C.

(d) Class B companies and mid-sized incumbent local exchange carriers, as defined by § 32.9000, that desire more detailed accounting may adopt the accounts prescribed for Class A companies upon the submission of a written notification to the Commission. Mid-sized incumbent local exchange carriers shall maintain subsidiary record categories necessary to provide the pole attachment data currently provided in the Class A accounts.

(e) The classification of a company shall be determined at the start of the calendar year following the first time its annual operating revenue from regulated operations equals, exceeds, or falls below the indexed revenue threshold.

6. Section 32.16 Changes in accounting standards is amended by revising paragraph (a) to read as follows:

§ 32.16 Changes in accounting standards.

(a) The company's records and accounts shall be adjusted to apply new accounting standards prescribed by the Financial Accounting Standards Board or successor authoritative accounting standard-setting groups, in a manner consistent with generally accepted accounting principles. The change in an accounting standard will automatically take effect 90 days after the company informs this Commission of its intention to follow the new standard, unless the Commission notifies the company to the contrary. Concurrent with informing this Commission of its intent to adopt an accounting standards change, the company shall also file a revenue requirement study for the current year analyzing the effects of the accounting standards change. Furthermore, any change subsequently adopted shall be disclosed in annual reports to this Commission.

(b) * * *

7. Section 32.23 Nonregulated activities is amended by revising paragraph (c) to read as follows:

§ 32.23 Nonregulated activities

* * * * *

(c) When a nonregulated activity does involve the joint or common use of assets and resources in the provision of regulated and nonregulated products and services, carriers shall account for these activities within accounts prescribed in this system for telephone company operations. Assets and expenses shall be subdivided in subsidiary records among amounts solely assignable to nonregulated activities, amounts solely assignable to regulated activities, and amounts related to assets and expenses incurred jointly or in common, which will be allocated between regulated and nonregulated activities. Carriers shall submit reports identifying regulated and nonregulated amounts in the manner and at the times prescribed by this Commission. Nonregulated revenue items not qualifying for incidental treatment as provided in §32.4999(1), shall be recorded in separate subsidiary record categories of Account 5280, Nonregulated operating revenue. Amounts assigned or allocated to regulated products or services shall be subject to part 36 of this chapter.

8. Section 32.2000 Instructions for telecommunications plant accounts is amended by revising subparagraph (4) of paragraph (a) and deleting the contents of paragraph (i) as follows:

§ 32.2000 Instructions for telecommunications plant accounts.

(a) * * *

(4) The cost of the individual items of equipment, classifiable to Accounts 2112, Motor vehicles; 2113, Aircraft; 2114, Special purpose vehicles; 2115, Garage work equipment; 2116, Other work equipment; 2122, Furniture; 2123, Office equipment; 2124, General purpose computers, costing \$2,000 or less or having a life of less than one year shall be charged to the applicable expense accounts, except for personal computers falling within Account 2124. Personal computers classifiable to Account 2124, with a total cost for all components of \$500 or less, shall be charged to the applicable Plant Specific Operations Expense accounts. If the aggregate investment in the items is relatively large at the time of acquisition, such amounts shall be maintained in an applicable material and supplies account until items are used.

(i) Reserved

9. Paragraph 32.2000(b)(4) is deleted.

10. Paragraph 32.2000(j) Plant accounts to be Maintained by Class A and Class B telephone companies is revised as follows:

* * * * *

(j) Plant Accounts to be Maintained by Class A and Class B telephone companies as indicated:

<u>Account Title</u>	<u>Class A Account</u>	<u>Class B Account</u>
----------------------	----------------------------	----------------------------

REGULATED PLANT

* * * * *

TELECOMMUNICATIONS PLANT IN SERVICE (TPIS)

TPIS-General Support assets:

Special purpose vehicles 2114 is renamed Tools and other work equipment 2114, and Garage work equipment 2115 and Other work equipment 2116 are deleted.

* * * * *

11. Section 32.2003 Telecommunications plant under construction is amended by revising paragraph (a) as follows:

§ 32.2003 Telecommunications plant under construction.

(a) This account shall include the original cost of construction projects (note also § 32.2000(c)) and the cost of software development projects that are not yet ready for their intended use.

12. Section 32.2114 Special purpose vehicles is renamed and revised to read as follows:

§ 32.2114 Tools and other work equipment.

This account shall include the original cost of special purpose vehicles and the original cost of tools and equipment used to maintain special purpose vehicles and items included in Accounts 2112 and 2113. This account shall also include the original cost of power-operated equipment, general purpose tools, and other items of work equipment.

13. Section 32.2115 Garage work equipment is deleted.

14. Section 32.2116 Other work equipment is deleted.

15. Section 32.2124 General purpose computers is amended by deleting paragraph (c) and revising paragraph (d) as follows:

§ 32.2124 General purpose computers.

* * * * *

(c) Reserved

(d) This account does not include the cost of computers and their associated peripheral devices associated with switching, network signaling, network operations, or other specific telecommunications plant. Such computers and peripherals shall be classified to the appropriate switching, network signaling, network expense, or other plant account.

16. Section 32.2311 Station apparatus is amended to revise paragraph (d) as follows:

§ 32.2311 Station apparatus.

* * * * *

(d) Operator head sets and transmitters in central offices and at private branch exchanges, and test sets such as those used by wire chiefs, outside plant technicians, and others, shall be included in Account 2114, Tools and other work equipment, Account 2220, Operator systems, or Account 2341, Large Private Branch Exchanges, as appropriate.

* * * * *

17. Section 32.2690 Intangibles is amended by revising paragraph (c) as follows:

§ 32.2690 Intangibles.

* * * * *

(c) The cost of other intangible assets, not including software, having a life of one year or less shall be charged directly to Account 6564, Amortization Expense - Intangible. Such intangibles acquired at small cost may also be charged to Account 6564, irrespective of their term of life. The cost of software having a life of one year or less shall be charged directly to the applicable expense account with which the software is associated.

18. Section 32.3500 Accumulated amortization - intangible is amended by revising paragraph (c) and adding paragraph (d) as follows:

§ 32.3500 Accumulated amortization - intangible.

* * * * *

(c) When any item carried in Account 2690, other than software, is sold, relinquished, or otherwise retired from service, this account shall be charged with the cost of the retired item. Remaining amounts associated with the item shall be debited to Account 7360, Other Nonoperating Income.

(d) When software that is classified to Account 2690 is sold, relinquished, or otherwise retired from service, this account shall be credited, and Account 6564, Amortization expense - intangible, shall be charged with the unamortized cost of the existing software.

19. Section 32.4999 General is amended by revising paragraph (1) as follows:

§ 32.4999 General.

* * * * *

(l) *Nonregulated revenues.* The nonregulated revenue account shall be used for nonregulated operating revenues when a nonregulated activity involves the common or joint use of assets or resources in the provision of regulated and nonregulated products or services as required in § 32.23(c) of this subpart. Revenues from nontariffed activities offered incidental to tariffed services may be accounted for as regulated revenues, provided the activities are outgrowths of regulated operations and the revenues do not exceed, in the aggregate, one percent of total revenues for three consecutive years. Such activities must be listed in the Commission-approved Cost Allocation Manual for any company required to file a Cost Allocation Manual.

(m) * * *

(n) Revenue Accounts to be Maintained as indicated:

<u>Account Title</u>	<u>Class A Account</u>	<u>Class B Account</u>
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Local Network Services Revenues:

Public telephone revenue 5010 is deleted.

20. Section 32.5010 Public telephone revenue is deleted.

21. Section 32.5280 Nonregulated operating revenue is amended by revising paragraph (a) as follows:

§ 32.5280 Nonregulated operating revenue.

(a) This account shall include revenues derived from a nonregulated activity involving the common or joint use of assets or resources in the provision of regulated and nonregulated products or services.

22. Section 32.5999 General is amended by revising paragraph (f)(5) and (h) as follows:

§ 32.5999 General.

* * * * *

(f)(5) *Clearances.* This subsidiary record category shall include amounts transferred to Construction accounts (see § 32.2000(c)(2)(iii)), other Plant Specific Operations Expense accounts and/or Account 3100, Accumulated Depreciation (cost of removal; see § 32.2000(g)(1)(iii)), as

appropriate, from Accounts 6112, Motor vehicles expense, 6114, Tools and other work equipment expense, 6534, Plant operations and administration expense, . . .

(g) * * *

(h) *Expense accounts to be maintained.*

<u>Account Title</u>	<u>Class A Account</u>	<u>Class B Account</u>
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INCOME STATEMENT ACCOUNTS

Plant specific operations expense:

Special purpose vehicles expense 6114, is renamed Tools and other work equipment expense 6114. Garage work equipment expense 6115 and Other work equipment expense 6116 are deleted.

* * * * *

23. Section 32.6110 Network support expenses is amended by revising paragraph (a) as follows:

§ 32.6110 Network support expenses.

(a) This account number shall be used by Class A telephone companies to summarize for reporting purposes the contents of Accounts 6112 through 6114. Class B telephone companies shall use this account for expenses of the type and character required of Class A companies in Accounts 6112 through 6114.

(b) * * *

24. Section 32.6114 Special purpose vehicles expense is renamed and revised to read as follows:

§ 32.6114 Tools and other work equipment expense.

(a) This account shall include costs incurred in connection with special purpose vehicles, garage work equipment and other work equipment included in Account 2114, Tools and other work equipment. This account shall be charged with costs incurred in connection with the work equipment itself. This account shall also include such costs as fuel, licenses and inspection fees, washing, repainting and minor accessories. The costs of using garage work equipment to maintain motor vehicles shall be charged to Account 6112, Motor vehicles expense. This account shall not be charged with the costs of operators of special purpose vehicles and other work equipment. The costs of operators of this equipment shall be charged to accounts appropriate for the activities performed.

(b) Credits shall be made to this account for amounts related to special purpose vehicles and other work equipment transferred to Construction and/or to other Plant Specific Operations Expense accounts. These amounts shall be computed on the basis of direct labor hours. (See also § 32.5999(f)(5) of this subpart.)

25. Section 32.6115 Garage work equipment expense is deleted.

26. Section 32.6116 Other work equipment expense is deleted.

27. Section 32.6124 General purpose computers expense is amended by revising the section as follows:

§ 32.6124 General purpose computers expense.

This account shall include the costs of personnel whose principal job is the physical operation of general purpose computers and the maintenance of operating systems. This excludes the cost of preparation of input data or the use of outputs which are chargeable to the accounts appropriate for the activities being performed. Also excluded are costs incurred in planning and maintaining application systems and databases for general purpose computers. (See also Account 6724, Information Management.) Separately metered electricity for general purpose computers shall also be included in this account.

28. Section 32.6724 Information management is amended by revising the section as follows:

§ 32.6724 Information management.

This account shall include costs incurred in planning and maintaining application systems and databases for general purpose computers.

29. Paragraph 32.9000, Glossary of terms is revised to include the following definition, between the definitions of *intrasystems* and *minor items*:

§ 32.9000 Glossary of terms.

Mid-sized incumbent local exchange carrier is a carrier whose operating revenue equals or exceeds the indexed revenue threshold and whose revenue when aggregated with the revenues of any local exchange carrier that it controls, is controlled by, or with which it is under common control is less than \$7 billion. Each of these local exchange carriers would be eligible for Class B accounting, except as noted in § 32.11(b) and (d), even if the annual operating revenue of any individual local exchange carrier exceeds the indexed revenue threshold (see definition for indexed revenue threshold in this section).

Part 64 of Title 47 of the C.F.R. is amended as follows:

PART 64 - MISCELLANEOUS RULES RELATING TO COMMON CARRIERS

30. The authority citation for Part 64 continues to read as follows:

Authority: 47 U.S.C. 10, 201, 218, 226, 228, 332, unless otherwise noted.

31. Paragraph 64.904(a) is revised to read as follows:

§ 64.904 Independent audits.

(a) With the exception of mid-sized local exchange carriers each local exchange carrier required to file a cost allocation manual, by virtue of having annual operating revenues that equal or exceed the indexed revenue threshold for a given year or by order by the Commission, shall have an audit performed by an independent auditor on an annual basis, with the initial audit performed in the calendar year after the carrier is first required to file a cost allocation manual. The audit shall provide a positive opinion on whether the applicable data shown in the carrier's annual report required by § 43.21(e)(2) of this chapter present fairly, in all material respects, the information of the carrier required to be set forth therein in accordance with the carrier's cost allocation manual, the Commission's Joint Cost Orders issued in conjunction with CC Docket No. 86-111 and the Commission's Accounting Safeguards proceeding in CC Docket No. 96-150 and the Commission's rules and regulations including §§ 32.23 and 32.27 of this chapter, 64.901, and 64.903 in force as of the date of the auditor's report. The audit shall be conducted in accordance with generally accepted auditing standards, except as otherwise directed by the Chief, Common Carrier Bureau.

32. Paragraph 64.904(b) is renumbered as 64.904(c)

33. A new Paragraph 64.904(b) is added as follows:

§ 64.904 Independent audits.

* * * * *

(b) A mid-sized incumbent local exchange carrier, as defined in §32.9000, required to file a cost allocation manual, shall have an attest engagement performed by an independent auditor every two years covering the two year period, with the initial engagement performed in the calendar year after the carrier is first required to file a cost allocation manual. The attest engagement shall be an examination engagement and shall provide a written communication that expresses an opinion that the results reported pursuant to 43.21(e)(2) of this chapter are an accurate application of the Commission's Joint Cost orders issued in conjunction with CC Docket No. 86-111 and the Commission's Accounting Safeguards proceeding in CC Docket No. 96-150 and the Commission's rules and regulations including §§32.23 and 32.27 of this chapter, 64.901 and 64.903 in force as of

the date of the auditor's written report. The written communication shall also express an opinion that the cost methodologies in place are in conformance with the cost allocation manual filed with the Commission. The attest engagement shall be conducted in accordance with the attestation standards established by the American Institute of Certified Public Accountants, except as otherwise directed by the Chief, Common Carrier Bureau.

* * * * *

SEPARATE STATEMENT OF COMMISSIONER SUSAN NESS***Re: ITTA Petition for Forbearance***

We are in the middle of a turbulent period as we transition from monopoly to competition. Many rules -- and even statutory provisions -- that were put into place during a monopoly regime may no longer be necessary to effectuate their intended purpose.

Recognizing that the marketplace is rapidly evolving, Congress wisely provided the Commission with a flexible tool to forbear from enforcement of provisions of law and regulations where the Commission finds it serves the public interest to do so.

The forbearance petition filed by the Independent Telephone and Telecommunications Alliance (ITTA) affords us an opportunity to review particular rules to determine whether they continue to be necessary to serve the public interest. The petition requests regulatory relief for mid-sized local exchange carriers that serve less than two percent of the nation's access lines.

Under a section 10 forbearance analysis, the Commission must forbear from applying any rule or regulation if the Commission determines that (1) enforcement is not necessary to ensure that charges and practices are just and reasonable, (2) enforcement is not necessary for the protection of consumers, and (3) forbearance is consistent with the public interest.

In a series of orders, we grant the forbearance requested in some instances; we go beyond what was requested in some instances by providing relief to a broader class of carriers; and in a few limited instances we conclude that continued enforcement is necessary for the protection of consumers.

One request that the majority does not grant is forbearance from the Commission's requirement that incumbent local exchange carriers offer certain services through separate affiliates. While our separate affiliate rules have served a very important purpose in the past, separation may be less essential as competition evolves. Based on the record in this proceeding, however, I am not convinced that competition has developed to the point where consumers will be adequately protected if we forbear from our rules. I look forward to working with the parties to develop a better record and to determine whether structural separation promotes competition or detracts from the competitive market place.

**CONSOLIDATED SEPARATE STATEMENT OF
COMMISSIONER HAROLD FURCHTGOTT-ROTH**

*Re: Petition for Forbearance of the Independent Telephone & Telecommunications Alliance;
Regulatory Treatment of LEC Provision of Interexchange Services Originating in the LEC's
Local Exchange Area*

I support these items to the extent that they provide the relief requested by the Independent Telephone & Telecommunications Alliances (ITTA) petition. I object, however, to the extent that the regulatory relief requested is denied or some lesser regulatory relief is provided. Moreover, I question the overall approach that the Commission has taken to this forbearance petition.

I start with the presumption that the ITTA petition has been "deemed granted" in full because of the Commission's failure either (i) to deny the petition within one year after receiving it, or (ii) to make an explicit finding that a 90 day extension was necessary to meet the statutory requirements. Section 10 of the Communications Act is very clear: "The Commission may extend the initial one-year period by an additional 90 days if the Commission finds that an extension is necessary to meet the requirements of subsection (a)." The statute is thus specific that it is the "Commission" which must grant any extension and must do so upon a finding that the extension is necessary to meet the purposes of section 10(a). I do not believe that the bureau, acting on its own motion and without even prior consultation with the "Commission," can act to extend this statutory time-frame. I do not believe that the 90 day extension can be effectively used by the bureau without even briefing the Commission on the merits of the underlying petition, determining whether or not there are any new or novel questions of fact, law or policy, and receiving some signal from a majority of the "Commission" that an extension of time is warranted under these particular circumstances.

In addition, I disagree with several aspects of the approach that the Commission has taken to this forbearance petition. In several instances, the Commission determines that ITTA has not met the criteria for forbearance to the extent that the petition requests relief beyond that which is granted in a contemporaneous rulemaking proceeding. *See e.g.*, Petition for Forbearance of the Independent Telephone & Telecommunications Alliance, Third Memorandum Opinion and Order in AAD File No. 98-43, at para. 10 (denying relief to the extent that petition "extends beyond the relief granted in the *LEC Classification Second Order on Reconsideration*."). *See also*, Petition for Forbearance of the Independent Telephone & Telecommunications Alliance, Sixth Memorandum Opinion and Order in AAD File No. 98-43, at para. 2 ("Although we do not grant forbearance from our rules regarding applications for special permission at this time, we are considering whether, and how, we should modify some of our rules that necessitate applications for special permission as part of our ongoing biennial review rulemaking and expect to make a final decision on the basis of that more complete record in the near future."). I am troubled that the Commission has decided to provide some lesser form of regulatory relief than that which was requested -- doing so in a separate rulemaking where the Commission has more discretion -- and then has used that proceeding as part of the justification for denying full regulatory forbearance as requested. In other words, the Commission has determined that the simplest method of dealing with these petitions is to deny the forbearance relief at issue while at the same time providing lesser relief in a separate rulemaking proceeding. But that is not the process the statute requires. Moreover, under such an approach, the Commission is able to avoid the

difficult question of why, when considering the same facts, particular regulatory relief is appropriate and other regulatory relief would contravene the statute. Such distinctions would frequently be difficult to justify as the forbearance criteria focus on general standards -- e.g. "protection of consumers," or "in the public interest." I object to the Commission's attempt to avoid the objective rigor of the section 10 forbearance test by providing regulatory relief in separate proceedings where the Commission has more discretion.

In addition, this approach lends itself to eliminating one set of requirements and at the same time adopting new -- albeit lesser -- regulatory restrictions that would not be justified under section 10 alone. *See e.g.*, Biennial Regulatory review of Accounting and Cost Allocation Requirements, Petition for Forbearance of the Independent Telephone & Telecommunications Alliance, Fourth Memorandum Opinion and Order in AAD File No. 98-43, at par. 25 (reinterpreting ITTA petition as not asking to forbear from Class A accounting altogether but "[e]ssentially . . . asking us to change our rules, not to forbear from applying the current rules."). While section 10 provides that the Commission may be able to forbear "in whole or in part" from a particular provision or regulation, *see* section 10(c), it does not provide the Commission with any authority to *adopt* new regulations or to *impose* separate conditions in the context of a forbearance petition. Section 10's primary emphasis is on deregulation, and I will not support this provision, or any of the proceedings required by a section 10 petition, being used as an opportunity to authorize new regulatory restrictions or conditions. I fear that this type of expansive reading of the Commission's authority under the Act's forbearance provisions will lead the Commission astray from its clear statutory duties and limitations.

Finally, as I have stated previously, I am concerned that the Commission is placing too high a burden on the parties requesting forbearance relief. I believe that the Section 10 forbearance scheme requires the Commission to justify continued regulation in light of the competitive conditions in the marketplace. The Commission cannot meet their statutory obligations by simply shifting the burden to petitioners to justify forbearance.

SEPARATE STATEMENT OF COMMISSIONER MICHAEL K. POWELL

Re: Petition for Forbearance of the Independent Telephone and Telecommunications Alliance (AAD File No. 98-43), *and related proceedings* (CC Docket No. 97-11, CC Docket No. 98-81, CC Docket No. 96-150, CC Docket No. 98-117, WT Docket No. 96-162, CC Docket No. 96-149, CC Docket No. 96-61)

I am pleased to join my colleagues in granting some of the regulatory relief requested in the forbearance petition filed by the Independent Telephone and Telecommunications Alliance (ITTA) on behalf of mid-sized local exchange carriers. Although I concur in the results of most of these items (especially where regulatory relief is granted), I am, however, compelled to dissent in part to three of the decisions, and I continue to be concerned about the Commission's handling and analysis of forbearance requests under section 10 of the Communications Act.

In these various items (some concern other ongoing rulemaking proceedings), we address nine regulatory requirements from which ITTA, on behalf of mid-sized LECs, requested forbearance. We adopted seven different Orders in response to the petition (and other petitions or notices). In looking at these Orders as a package and individually, while some relief is granted, I continue to be concerned that, where forbearance is denied, these petitions are not being treated in a manner fully consistent with the intent and spirit of section 10 of the Act. While I concur with the outcome of most of these items -- since I believe we are reaching the correct result -- I do continue to question (along lines similar to those I have expressed elsewhere) our means and methods for handling forbearance petitions.

I must respectfully dissent, however, from the continued application of separate affiliate requirements for the provision of in-region interexchange services and commercial mobile radio services (CMRS) by mid-sized LECs. My reasons are twofold. First, I continue to be uneasy with the degree to which reliance on this and similar regulatory devices is based on speculation about anticompetitive behavior. I fully understand that any analysis about potentially harmful future conduct entails some assessment of likely conduct. Historically, the agency has stewarded the basic principle of nondiscrimination, resulting in regulatory protections against cost misallocation and anticompetitive behavior flowing from control of a "bottleneck" facility. Our precedents, such as separate affiliate requirements, were rightly premised on the existence of a true monopolist (sanctioned by the state) and the associated risks. In that environment, not only did the incumbent have monopoly power, there was no prospect of competition nor any watchful present or future competitors. These safeguards were designed to protect consumers from the potential ill effects of such accumulated power.

I believe, however, that much has changed. The movement toward a competitive environment means that we must take into fuller consideration the necessity, viability, and the potentially distorting competitive-consequences of old familiar regulatory devices. Thus, to the extent we must speculate about potential harm (to competition and consumers) we must, too, factor in more fully the potential disciplining effects of both real competition and potential competition. I see a continued tendency to invoke the ancient mantra "to protect against discriminatory this or that" as glib justification for continued regulatory constraints. I believe we must work harder and press more heavily on the traditional rationales. I do not believe we did so in this case. Moreover, to do so will

take time and resources, which we do not have when forbearance petitions are presented for deliberation with only a second or two left on the statutory shot-clock, as was the case here.

My second concern rests with the extent that the Commission expresses a tendency to justify certain regulatory restrictions in the name of promoting or advancing competition. That alone, of course, may be worthy, but we are not free to do so in a manner that involves intermediate judgements that differ from those reached by Congress. Let me explain more fully.

Prior to the 1996 Act, I believe both Judge Greene and the FCC did seek to create limited competitive markets out of the monopoly provider's control and, concomitantly, impose safeguards designed to keep the monopolist from thwarting fledgling competitors as well as ensuring that core regulatory goals were not compromised by such competitive forays. These competitive excursions were limited and usually merely incremental voyages into competitive service markets. But, we must be reminded that the fundamental paradigm remained regulation and central control over the most prized services. The key point is that Judge Greene and the Commission had a fairly wide birth to develop the conditions of their market-opening efforts.

The 1996 Act, however, altered the paradigm and structured the basic terms of competition. Competitive services were to become the rule, and regulated services the limited exceptions. By its act, Congress crafted a comprehensive competitive model, designed specifically to supplant the MFJ. In weaving this fabric, Congress made a number of significant judgements. The one most relevant here is that it concluded that, rather than restrict the ILECs to regulated wholesale service, it allowed ILECs to compete at the retail level as well. This judgement may prove unwise or unworkable, but it is the one that Congress chose.

Congress was not oblivious to the challenges or perils of allowing the ILECs to compete, however, in long distance and other services while they still controlled many of the necessary facilities and inputs that other competitors would need. It addressed this problem by crafting an access and interconnection regime (sections 251 and 252) that placed unique duties and obligations on ILECs. In addition, Congress recognized that different classes of LECs required different levels of safeguards and incentives. Bell Operating Companies (BOCs), and they alone, are subject to sections 271 and 272. ILECs have more duties and obligations than CLECs, and so on. Thus, whether one likes it or not, *Congress* substantially addressed the dangers of "bottleneck control" and discriminatory incentives in the Act.

As a consequence, I believe, the Commission is not as free (as it perhaps was prior to the Act) to steward a transition to a competition regime different than that of the one chosen by Congress. Specifically, as it relates to the question of separate affiliates, we must be careful not to impose regulatory requirements that in practical effect amount to wholesale/retail separations, where Congress intended none. (I note that in contrast to the carriers petitioning here, BOCs are expressly subject to separate affiliates for some services). For this reason, I am uncomfortable with the analysis proffered to support continued separate affiliate requirements. We cite "bottlenecks" and "incentives" in what subtly (though perhaps unintentionally) seems to me a preference for wholesale separation in a competitive market. By way of illustration, the Orders often speak of the importance of separate affiliates to ensure that they obtain facilities on an "arm's length basis" and to ensure that all competing in-region providers and other carriers have the same access (*i.e.*, wholesale).

Though Congress made judgements about the competitive ground-rules, it did not endeavor to sweep through our regulations and apply those judgments to each and every structural requirement on the books. Instead, it directed us to search out such rules and apply the new paradigm. To do so, it gave the Commission the twin engines of the biennial review and forbearance. This is one reason I believe that section 10 is important in evaluating the continued validity of separate affiliate requirements, not otherwise mandated by law, where competitive conditions and/or other regulatory or enforcement mechanisms are already in place.

I believe that the petition before us raised substantial questions with regard to the need for structural separation in light of present conditions. Accordingly, I believe that in response to ITTA's forbearance petition, we should have examined more carefully alternative methods of enforcing core ILEC responsibilities to see if there wasn't a more rational, limited approach. For example, we should have explored including a sunset of the structural separation requirement for in-region interexchange services like that available to BOCs in section 272 and treating mid-sized LECs more like rural carriers under the CMRS separate affiliate requirement.

For these reasons, I respectfully dissent in part from these particular decisions.